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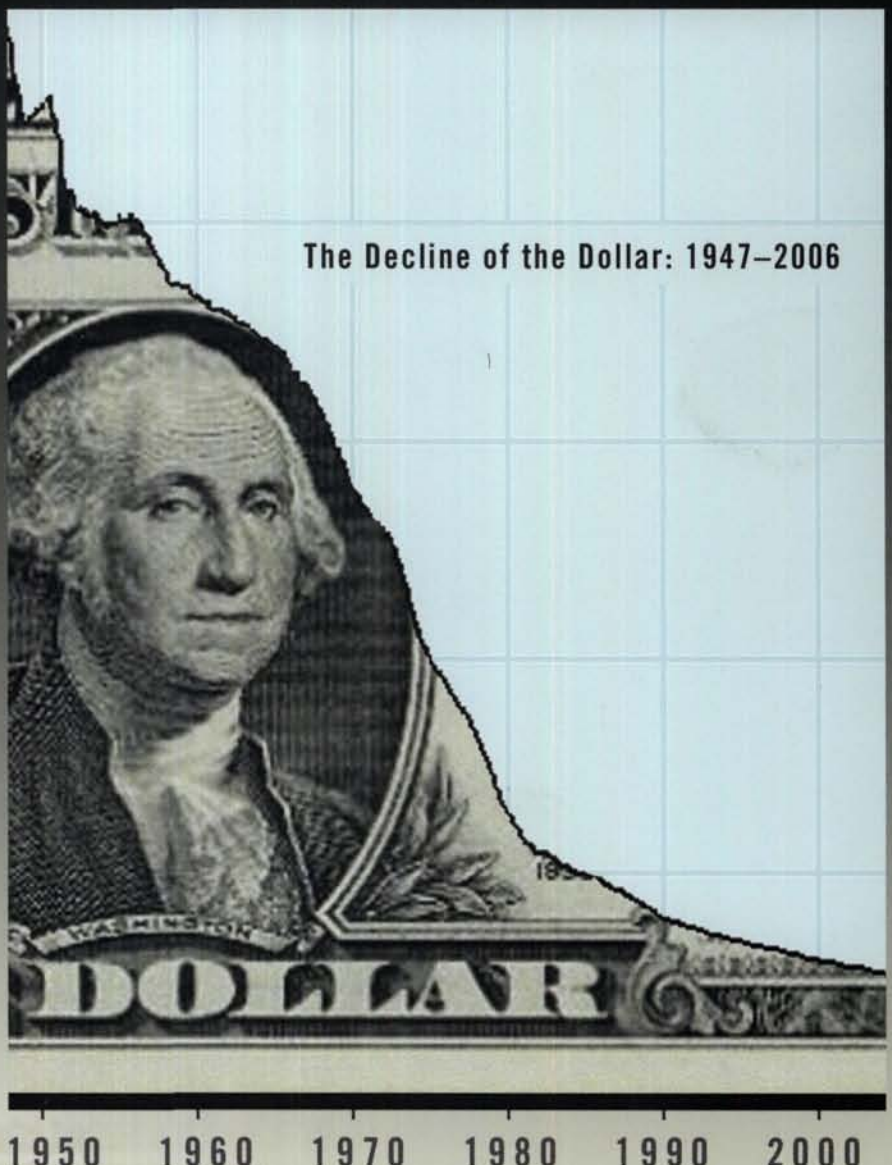

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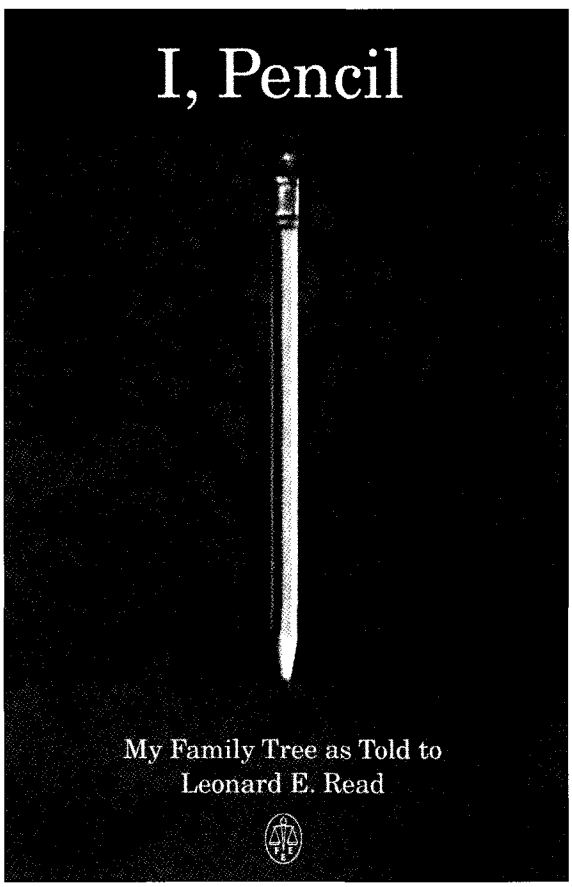

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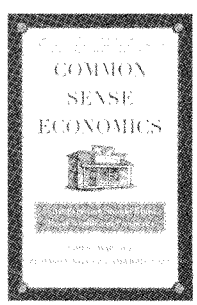

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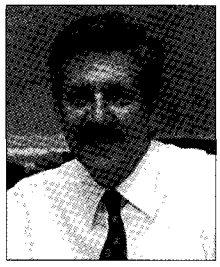
Freedom and the Pitfalls of Predicting the Future



BY RICHARD M. EBELING

The prospects for freedom in America and in many other parts of the world appear dim. Government continues to grow bigger and more intrusive, imposing tax burdens that siphon vast amounts of private wealth. Extrapolating these trends out for the foreseeable future, it would seem that the chances for winning liberty are highly unlikely. There is only one problem with this pessimistic forecast: the future is unpredictable and apparent trends do change.

Many years ago the famous philosopher of science Karl Popper pointed out, "If there is such a thing as growing human knowledge, then we cannot anticipate today what we shall only know tomorrow." What does this mean? When I was in high school in the 1960s, I came across an issue of *Popular Science* magazine published in the late 1940s that was devoted to predicting what life would be like for the average American family in the 1970s. On the cover was a picture of a wife and children standing by a white picket fence waving goodbye to dad as he went off to work—in his one-seat minihelicopter!

Inside, as best as I can recall, the authors talked about such things as color televisions, various new household appliances, robots that would do much of our work, and the use of jet planes for commercial travel. What was not mentioned, however, was the personal computer or the revolution in communication, knowledge, and work that it has brought about. When that issue of *Popular Science* was published, one essential element of the computer revolution had not yet been invented: the microchip.

Those authors could not imagine a worldwide technological revolution before the component that made it all possible was created by man. Our inescapably imperfect knowledge means we can never predict our own future. If we could predict tomorrow's knowledge and its potentials, then we would already know everything today—and we would know we knew it!

This applies to social, political, and economic trends as well. Most people in 1900 expected the twentieth century to be an epoch of growing international peace and harmony. In 1911 Norman Angell argued in *The Great Illusion* that war had become so costly that it would be irrational to be drawn down that path any longer. But, instead, the past century was the bloodiest and most destructive in history due to the rise of political and economic collectivism. The conflicts that collectivism brought in its wake have cost possibly 250 million lives over the last 100 years. No one anticipated this turn of events when the century began.

When I was an undergraduate in the late 1960s the textbook assigned in my first economics class was the seventh edition of Paul Samuelson's *Economics* (1967). There was a graph that tracked U.S. and Soviet Gross National Product (GNP) from 1945 to 1965. Samuelson then projected American and Soviet GNP through the rest of the century. He anticipated that possibly by the early 1980s, but certainly by 2000, Soviet GNP would be equal to or even greater than that of the United States. Notice his implicit prediction that there would be a Soviet Union in 2000.

Which of us *really* expected to see the end of the U.S.S.R. in our lifetimes, without either a nuclear cataclysm or a devastating and bloody civil war? In the mid-1980s the often perceptive French social critic Jean-François Revel (who died in April) published *How Democracies Perish*, in which he expressed his fear that the loss of moral and ideological commitment to freedom by intellectuals and many other people in the West meant that the global triumph of communism under Soviet leadership was a strong possibility. Instead it was Soviet communism that disappeared from the map.

Who in January 1990 anticipated that Saddam Hussein would invade Kuwait in August of that year, setting in motion a chain of events that has now resulted in two

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American invasions of Iraq? Who in 2000 would have anticipated that Bill Clinton's eight years in office would seem, in retrospect, an era of restrained government compared to the explosion in government spending and intervention during the current Bush administration?

And who today knows what the 21st century holds for us? Let me suggest that the answer is: nobody. As the late Robert Nisbet, one of America's great social thinkers, once pointed out, "How easy it is, as we look back over the past—that is, of course, the 'past' that has been selected for us by historians and social scientists—to see in it trends and tendencies that appear to possess the iron necessity and clear directionality of growth in a plant or organism. . . . But the relation between the past, present, and future is chronological, not causal."

The decades of relative global peace and prosperity that preceded 1914 did not mean that war and destruction were impossible for the rest of the twentieth century. The ascendancy of Soviet communism and German fascism in the 1930s and 1940s did not mean that freedom and democracy had reached their end. And the persistent and current growth in government intervention and the welfare state does not mean that a return to the classical-liberal ideas of individual liberty, free markets, and limited government is a pipe dream of the past.

Human events are the result of human action. Our actions are an outgrowth of our ideas. The stranglehold of Big Government will persist only for as long as we allow it, for as long as we accept the arguments of our ideological opponents that the interventionist welfare state is "inevitable" and "irreversible." That is, the present trend will continue only for as long as we accept that the chronologically observed increase in government power over the last decades is somehow causally determined and inescapable in the stream of human affairs.

This could have been equally said about slavery. Few institutions were so imbedded in the human circumstance throughout recorded history as the ownership of some men by others. Surely it was a pipe dream to suggest that all men should be free and equal before the law. Yet in the eighteenth and nineteenth centuries a new political ideal was born—that all men are created equal and endowed by their Creator with certain unalienable rights, which no other mortals could take away. So slavery, which Aristotle considered to be the natural condition of some men, was brought to an end before the close of the nineteenth century.

Mercantilism's Grip

In the 1700s, mercantilism—the eighteenth-century version of central planning—was considered both necessary and desirable for national prosperity. Even Adam Smith, in the *Wealth of Nations*, believed that its hold over men's minds and actions was too powerful to ever permit the triumph of free trade. Yet in one lifetime following Smith's death in 1790, freedom of trade and enterprise was established in Great Britain and the United States, and then slowly but surely through much of the rest of the world.

We cannot imagine how freedom will prevail over paternalistic government, any more than people could imagine in 1940 a world without Nazism and Soviet communism, or FDR's New Deal. But that does not mean it's impossible.

Precisely because the future is unknown, we may be confident that trends can and will change. We cannot know today what arguments friends of freedom will imagine and successfully articulate tomorrow to end government control of our lives. But those arguments are out there, waiting to be discovered and presented, just as earlier friends of freedom succeeded in making the case against slavery and mercantilism. As Austrian economist Ludwig von Mises pointed out in *The Freeman* in 1951, "Now trends of [social] evolution can change, and hitherto they almost always have changed. But they changed only because they met firm opposition. The prevailing trend toward what Hilaire Belloc called the servile state will certainly not be reversed if nobody has the courage to attack its underlying dogmas." There is one thing, therefore, that we can predict: patience, persistence, and belief in the power of ideas will provide the best chance we have to achieve the free society we so much desire.

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Perspective

Jane Jacobs (1916–2006)

On the second page of her first book, *The Death and Life of Great American Cities* (1961), which has become a classic, Jane Jacobs wrote:

> There is a wistful myth that if only we had enough money to spend—the figure is usually put at a hundred billion dollars—we could wipe out all our slums in ten years, reverse decay in the great, dull, gray belts that were yesterday's and day-before-yesterday's suburbs, anchor the wandering middle class and its wandering tax money, and perhaps even solve the traffic problem.
>
> But look what we have built with the first several billions: Low-income projects that become worse centers of delinquency, vandalism and general social hopelessness than the slums they were supposed to replace. Middle-income housing projects which are truly marvels of dullness and regimentation, sealed against any buoyancy or vitality of city life. Luxury housing projects that mitigate their inanity, or try to, with a vapid vulgarity. Cultural centers that are unable to support a good bookstore. Civic centers that are avoided by everyone but bums, who have fewer choices of loitering place than others. Commercial centers that are lackluster imitations of standardized suburban chain-store shopping. Promenades that go from no place to nowhere and have no promenaders. Expressways that eviscerate great cities. This is not the rebuilding of cities. This is the sacking of cities.

Almost midway through the book, she wrote, "Although it is hard to believe, while looking at dull gray areas, or at housing projects or at civic centers, the fact is that big cities *are* natural generators of diversity and prolific incubators of new enterprises and ideas of all kinds. . . . The diversity, of whatever kind, that is generated by cities rests on the fact that in cities so many people are so close together, and among them contain so many different tastes, skills, needs, supplies, and bees in their bonnets. . . . The diversity of city enterprises includes all degrees

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of size, but great variety does mean a high proportion of small elements. A lively city scene is lively largely by virtue of its enormous collection of small elements."

And therein lies a city's greatness, as Jacobs spent so many years teaching us so eloquently. Through nearly a dozen books, Jacobs made an indelible contribution to our understanding of what makes cities vibrant and what makes them dull. She struck heroic blows in defense of the "underlying order of cities" and against the pretensions of social engineering. Alas, she died April 25 at age 89.

Although no advocate of laissez faire, Jacobs was critical of city planners because in seeking models, they looked to "anything but cities themselves." But of course. Who needs city planners if they are going to base their plans on actual cities? How do you plan spontaneity? You can't. So they brought "order by repression of all plans but the planners'."

With her sharp eye she noticed that "In city after city, precisely the wrong areas, in the light of planning theory, are decaying. Less noticed, but equally significant, in city after city the wrong areas, in the light of planning theory, are refusing to decay." Jacobs reminds me of the late Peter Bauer, the development economist. Like Bauer, Jacobs really cared about people, and because of this she was exquisitely sensitive to how they actually live and to the prerequisites for the fulfillment of *their* aspirations.

People are so much smarter living day to day in the microworld than they are designing the macroworld. The rationalism of the social engineer's laboratory is a curse that has brought untold misery. A popular slogan goes, "Think globally, act locally." Jacobs's work suggests a better if less romantic one: "Take care of the micro and the macro will take care of itself."

It is our deep loss that there will be no more from Jane Jacobs.

★ ★ ★

In France, when a proposed change in labor law would have made it easier to fire—and hence hire—young workers, students and union activists took to the streets in protest. Just a typical day in France? Maybe, but Anthony de Jasay analyzes the issues.

After 18 years, Alan Greenspan retired as chairman of the Federal Reserve at the beginning of 2006, ending the second-longest tenure for that position. Roger Garrison puts Greenspan's central-banking era in perspective.

China continues to exhibit the bizarre combination of an ever-freer economic system and a highly centralized authoritarian political system. James Dorn looks at China's prospects for full freedom.

As the scope of legislation expands in the United States, the police have jurisdiction over more and more of our lives. Earlier Americans were not so trusting of those who patrolled their streets. Becky Akers draws the contrast.

Why do so many people talk free enterprise, but practice statism? Our *Freeman* 50th-anniversary FEE Timely Classic this month is a ringing call for consistency by Fred DeArmond.

Ludwig von Mises stands as a giant in twentieth-century political economy, both for his economic theory and his defense of liberty. Richard Ebeling completes his two-part article on Mises's contributions to freedom.

Here's what our columnists have come up with: Richard Ebeling warns against predicting the future. Donald Boudreaux celebrates the wisdom of H. L. Mencken. Stephen Davies discusses underdevelopment. Russell Roberts sees a way to overcome the welfare state. And Joseph Stromberg, reading some recent badmouthing of the anti-federalists and Articles of Confederation, ripostes, "It Just Ain't So!"

This issue's reviewers have been busy assaying tomes on foreign aid, capitalism, water markets, and economic theory.

—*Sheldon Richman*
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Nothing to Learn from the Antifederalists? It Just Ain't So!

BY JOSEPH R. STROMBERG

According to Paul Greenberg, writing in the *Washington Times* in late January, the dreaded Antifederalists and their Articles of Confederation are making a comeback. In particular, these miscreants dare to question executive power. He writes with patriotic horror—a horror that assumes as self-evident a partisan reading of American history, a reading force-fed to most of us in public school. On that view, the Antifederalists' return would be terrible indeed, since those gentlemen were a set of backward-looking rustics unwilling or unable to see the necessity of a strong central government to guarantee our "national" security. Their opposition to the Constitution under which we now allegedly live is all the proof needed.

In 1787 we had recently defeated the British Empire—*without* a strong central American government directing the struggle—but having succeeded, we are supposed to have been in greater peril than before.

Here, as in many instances, the winners wrote the history of the conflict. The "founders" made their own propaganda for themselves as the ultimate "greatest generation." A set of nationalist historians in New England carried this gospel into the early nineteenth century.

The winning side even chose the parties' labels: "Federalist" for centralizing nationalists, and the negative-sounding "Antifederalist" for defenders of genuine federalism.

In 1983 historian Michael Lienesch noted that standard-issue historians invariably abuse the Antifederalists; fashions change, and the indictment with them, but there is *always* an indictment against the Antifederalists. They were "too local," narrow of vision, afraid of the future, and unable to share the Federalists' "continental vision." They were "too democratic"; later, they were seen as "too undemocratic."

Thus Antifederalists were "men of little faith," as historian Cecelia Kenyon put it in 1955. But now it is 2006 and the idea of having *faith* in *this* government at *this* time is all played out. Thomas Jefferson, out of power, would thunder about binding officeholders down with "the chains of the constitution"—and a good idea, if the Constitution were anything more than a "rope of sand."

Over the long haul, pretty much *every* dire prediction made by the Antifederalists has proven correct, although some took longer than others for their realization; and yet the Antifederalists get no credit. Among the predictions were ongoing centralization, creation of artificial monied aristocracies, long-run effacement of the states, and even a federal war made on a state or a group of states.

The Federalists invented a structure they could dominate, pronouncing it republican, even "democratic," since the people (one or thirteen?) were *ultimately* sovereign. Very comforting.

Mr. Greenberg's attack on the Antifederalists is a mere occasion for deploying the much-mooted Unitary Executive theory. The founders, he asserts, would be upset to learn that the president is forced to go to a quickie, drive-through court (FISA) before carrying on much-needed surveillance. What a shameful climb-down from the bold presidential assertion and usurpation "intended" by Article II.

One need only look at the written work of recent Supreme Court nominees and the administration's famous torture memorialists to see the grand (and central) project: sustaining the absurdist Unitary Executive theory. That doctrine credits the presidency with more unknown, "implied," and "inherent" powers than a team of FDR, Truman, and Nixon could dream up on an

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especially ambitious day. And the torture memos provide an example of what all this alleged power is good for.

Well-meaning constitutional traditionalists may argue of course that the Constitution, as written, debated, and ratified has little to do with such Bonapartist notions. When the "paper" of 1787 was under discussion, its advocates repeatedly told Americans that it secured their liberties and property through sundry interlocking protections. The president would only execute the laws passed by Congress. Congress's acts would not be legally binding unless consistent with the Constitution. Powers were enumerated.

These restrictions and safeguards withered away rather quickly. Congress and the Court did their part, and presidents began pretending to have found a vast treasury of power lurking, hitherto unmarked, in "The executive power"—in the *phrase*, that is, in the *mere words* that begin Article II, now revealed as mystic chords of construction, if not memory.

In opposing the Constitution the Antifederalists were not mounting a positive defense of the Articles. The value of their critique lies precisely in the critique of the new model—advanced warnings of the many flaws in the Federalists' product. Not the least of the flaws was the presidency itself. The office as such entails a quadrennial, circus-like disruption of American life, promotes centralization and social tinkering, and licenses irresponsible foreign policies.

"Energy" certainly abounds in the executive, but we might have done better with a committee.

Founders as Neoconservatives

Mr. Greenberg asks us to think of the founders as "neo-conservatives." This is an insult that must not stand, however little one may respect the founders' work. Mr. Greenberg is really expounding the "dare theory" of American law. He *dares* us to believe that, constitutionally, one man, more or less elected, can legally initiate war and do pretty much anything that pops into his head as an alleged means of defending the United States and repelling attack, even attacks that have not happened yet and probably would not ever happen until or unless a whole array of unlikely intermediate steps should fall into place.

Thanks, but no thanks. We are not likely to believe such a proposition, in its fullness; nor need we affirm the goodness of such a system. If Greenberg persuades us that the original Constitution actually envisioned such unknowably large executive powers, we are free to conclude that it is something of a swindle and stands in need of serious retooling, revision, or replacement.

Perhaps a convention exceeding its instructions, as in 1787, could do the trick.

"Conservative" neo-monarchists have raised the stakes, and they may answer for any drastic conclusions drawn. Such conservatives concede the Antifederalist claim that the Constitution was *already* a dangerous consolidation of power. Of course we may read the Antifederalists as spelling out the *tendencies* that would necessarily arise under the new system, once their opponents exploited each and every constitutional ambiguity (as they ultimately did).

Neo-federalists may say that the Constitution does *not* grant power to do X and Y; but once the federal government does them and the courts affirm the deed, present-day Madisonians have no argument. They may gripe about usurpations or mistakes, but since those are never reversed, what good is Mr. Madison's creative tinkering now? The Antifederalists were far better prophets, even if they could be premature on the timing of outcomes they feared.

The Federalists were the irrational optimists. The first Congress effectively refuted Madison's famous argument in Federalist No. 10 about the "dilution of faction" in a larger political sphere. At this late date it is easy to resolve one's love-hate relationship with the *Federalist Papers* decisively in favor of hate. As the Virginia jurist Abel P. Upshur wrote in 1840, "the Federalist is defective in some important particulars, and deficient in many more."

In denouncing rejection of the energetic, God-like presidency as "Antifederalism," Greenberg has opened conceptual doors he might have left shut. Good.

I wish there *were* genuine Antifederalists on the horizon today. If Democrats should really move in that direction—more power to them. If you see any Democrats embracing the Articles of Confederation, by all means welcome them aboard.

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Belt and Braces in the Labor Market

BY ANTHONY DE JASAY

Having moved to a new neighborhood, you go every week to the likeliest-looking supermarket in the vicinity and buy the supplies you need. After a while, finding price, quality, and service reasonably good, you give the supermarket that has thus withstood the trial a standing order for a weekly delivery of a bag of groceries. After a year or so, you come to fancy another store and stop your standing order.

In these ambulance-chasing days of the contingent fee, a plaintiff can find lawyers to prosecute almost any suit, no matter how outrageously frivolous. The supermarket that lost your custom finds lawyers prepared to argue that after a trial period, you entered into a de facto contractual relation with the supermarket, which after a year of blameless service by the plaintiff you terminated unilaterally without good cause. The court is asked to order you to restore your custom to the plaintiff and pay it damages. As some sanity still subsists in the judicial system, the suit is thrown out.

Suppose, however, that your standing order was not for food sold by a supermarket, but for some form of labor service sold by a worker. Instead of an informal understanding that may or may not be construed as a contract, you enter into a formal contract with the worker who undertakes to provide a service in consideration of the wages you undertake to pay him. After a trial period the contract is to run indefinitely unless terminated by either party upon due notice. Up to this point the sale of labor functions very much like the sale of groceries, except that the putative contract under which the groceries were sold is replaced by a contract that exists as an ascertainable fact. Fundamentally, however, the two cases have much in common.

Many if not most people nowadays would retort, with subdued or open indignation, that human labor is not like bags of groceries; in the employment relation human dignity, human destiny, and well-being are at stake. Therefore it is fundamentally immoral to want to apply the principle of freedom of contract to labor without further ado, as if labor were merchandise like any other.

There are weighty arguments backing this indignation. Whether they are accepted or not, they deserve consideration. However, in no way do they go without saying, although public opinion and current political thought treat them as if they did. Not only must they be clearly announced, but their implications must also be spelt out. Probably the most important implication is what could fittingly be called the belt-and-braces principle of the labor market.

Like every exchange, the exchange of labor for money is protected, as it were, by a belt, the contract. Labor, it is argued, must additionally be protected by the braces of justification. In even plainer English, this means that in order to dismiss a worker, an employer cannot simply rely on the contract telling him that he can do so by giving notice that will, so to speak, unbuckle the belt. He must also contrive to unbutton the braces by dealing with a requirement of justification.

Two rival doctrines are applied by legal systems to the requirement of justification. In many legal systems, both coexist in an ad hoc mixture; in others one or the other predominates. The two opposing extremes where one doctrine clearly dominates the other are the Australian and the French labor codes. Since the recent

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"Work Choice" legislation in Australia, it is broadly speaking up to the worker to show that his dismissal lacks justification. The category of "unfair dismissal" requires proof of a sort. By implication, dismissal that is not shown to be unfair is fair and requires no justification beyond the terms of the contract itself. The employer is "innocent" until proved "guilty." At least some of Australia's brilliant economic performance is probably due to the intelligent reforms of its labor market in recent years.

The French doctrine, a source of great pride for the socialist parties, the labor unions, and the intellectual leaders of public opinion, broadly speaking puts the burden on the employer to show that he is justified in dismissing a worker. There is a presumption that all dismissal is unfair unless it is proved to be fair. The employer must prevail, in the first instance, in a labor court where equal numbers of union and employer representatives sit on the bench, and where in 2004 out of over 200,000 cases judged, 65 percent were decided in favor of the worker(s). Judgment took an average of 13 months. One-fifth of cases were appealed, taking on average another 32 months to be decided.

Hiring Deterrent

It does not take a die-hard free-market economist to see how the belt-and-braces job security this doctrine provides for the employee injects a strong dose of risk into the employer's commitment and how it deters him from hiring. The risk is particularly perverse in its effect when the employer seeks to shed labor for what are termed "economic" reasons, namely, when it no longer pays him to employ the worker(s) in question. Such grounds were generally rejected if the employer was making a profit, since he was patently able to afford to pay the employee's wages and did not literally need to dismiss him. This kind of jurisprudence was breached last year by a judgment of the highest French court of appeal, which recognized that a dismissal may be justified if the employer is still making money but has good reason to fear that he will make a loss unless he reduces his payroll. It remains to be seen whether this judgment will have much effect on future lower court judgments.

The iron-clad labor code, all of 2,600 pages long, is a major cause of France's chronic unemployment, whose trend rate has been steadily rising for the last 30 years, in step with the flowering of the welfare state and the steady leftward bias of both center-left and center-right governments. Unemployment has been hovering near 10 percent for years, with unemployment of the under-25s at the staggeringly high rate of 23 percent. It could reasonably be argued that the albeit relative security of employment that the severe job-protection laws provide for 90 percent of the French labor force is paid for by the frustration and insecurity suffered by the 10 percent who are unemployed. It would seem to make good sense for the 10 percent to turn against the 90 percent and clamor for the abolition or at least the relaxation of the belt-and-braces safety enjoyed by the latter in a labor market frozen stiff by counterproductive concern for "social justice." Yet anyone who expected so rational a reaction would be quite mistaken.

Most of the first quarter of 2006 in France was spent by the government trying to obtain public acceptance of a new law that would have made a breach in the labor code to favor the hiring of young people by making their firing during an initial two-year period easier. The prospective beneficiaries of the law fought against it tooth and nail even more ferociously than the traditional guardians of the belt-and-braces system, the labor unions, the socialists, and most of the media. As he has invariably done during his long political career, President Chirac backed down in the face of the rioting and threats of mayhem, disavowed his prime minister, and effectively scuttled the youth-employment law. The rest of 2006 looks like it will be spent in trying to calm down the young with the derisory palliatives, financed by the taxpayer, that have been hurriedly voted to replace the youth-labor law which provoked the rebellion by France's habitual rebels.

Once again it has been proved that where the political class is cowardly and the executive gutless, laws can be made by parliament but can be unmade by noisy activists, unruly adolescents, violent pickets, and a press and television that back them. This tiny media-backed minority has time and again learnt the lesson that threats of violence always work and victory is to the cheeky. It is a pity that their victory is a defeat for labor-market reform and hence makes unemployment even more stubbornly chronic and incurable.

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Mencken's Wisdom

BY DONALD J. BOUDREAUX

This year marks the 50th anniversary of the death of H.L. Mencken (1880–1956). I wish that this Bard of Baltimore had lived far longer—past the age of Methuselah—so that those of us born after World War II could have enjoyed his brilliant insights into the likes of the space race, Watergate, Gerald Ford's "Whip Inflation Now" buttons, Nancy Reagan's "Just Say No" campaign, the "HillaryCare" scare, and the current President Bush's big-government conservatism.

Those who know Mencken's writings realize that he would have guffawed at such a wish. Mencken, after all, was the consummate realist. He was mature in the best sense of the word, seeing reality as clearly as any human being can see it, reporting what he saw and not what he imagined, avoiding fantasies no matter how wonderful they would be if they were reality, and refusing to fall for any and all crackpots and their schemes.

H. L. Mencken
Enoch Pratt Free Library, Baltimore

Mencken was and remains, in my opinion, America's greatest writer—one whose energetic style perfectly complemented his extensive learning and deep wisdom.

Here are four of my favorite Menckenisms.

> The most dangerous man, to any government, is the man who is able to think things out for himself, without regard to the prevailing superstitions and taboos. Almost inevitably he comes to the conclusion that the government he lives under is dishonest, insane and intolerable. . . . The average man, whatever his errors otherwise, at least sees clearly that government is something lying outside of him and outside the generality of his fellow men—that it is a separate, independent and often hostile power, only partly under his control, and capable of doing him great harm. (*A Mencken Chrestomathy*, pp. 145–146)

Mencken is correct about the kind of person most antagonistic to the state. Someone who thinks for himself neither needs nor welcomes someone else to think for him. And this person's independence of mind puts him on guard against the widespread superstition that government can perform miracles—miracles such as reducing the cost of some good simply by declaring that it may not be sold at a price higher than one specified by the government.

Unfortunately, I worry that Mencken's description of the "average man" is no longer valid. Does today's average American regard government as "something lying outside of him"? On specific issues, the answer is yes. Gun-control advocates, for example, regard Congress's failure to outlaw gun ownership as the choice not of some collective entity deserving respect but rather as the result of pernicious influences on the body politic. But the general attitude seems to be that government is us—that when government acts, it is us acting collectively—that the only, or most real, instance of our doing anything is when government acts in our name.

Reflect how often you encounter the phrase "we as a nation." "We as a nation" have chosen to fight a war on drugs. "We as a nation" cruelly abandoned poor people to Katrina's flood waters. "We as a nation" should regulate coal mines more strictly. And on and on.

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We as a nation need Mencken to remind us that we are individuals.

> The kind of man who demands that government enforce his ideas is always the kind whose ideas are idiotic. (*A Mencken Chrestomathy*, p. 622)

This insight is among my very favorites. Being sensible, sensible ideas seldom must be imposed by force. Sometimes sensible ideas are implemented gradually, as practices with widespread advantages displace less-advantageous practices and become part of customary behavior. Sometimes sensible ideas are adopted consciously and quickly, through the art of persuasion or the rigors of scientific demonstration.

In contrast, idiotic ideas have nothing going for them. Most people who voluntarily adopt idiotic ideas soon abandon them if these ideas hamper the ability to thrive in the real world. The only way to implement an idiotic idea widely and surely is through force.

Protectionism, for example, is a truly idiotic idea, premised on the ridiculous notion that a division of labor extending across political boundaries makes us poorer. If the CEO of General Motors travels the country trying to sell this idea—trying to persuade Americans to "buy American"—some people might fall for this plea. But most of us, when spending our own money, will take the best deals we find regardless of the nationality of those offering the deals. The result is greater prosperity.

So protectionism's only hope for taking root is for it to be imposed by force. Such is the glory of idiotic ideas.

But matters get worse: as force comes to be more widely accepted (itself a stupendously idiotic idea!), people have less and less incentive to reject their defective ideas in favor of sensible ones. With government standing ready to rent its force to the highest bidders, the politically influential can now more reliably force their idiotic notions on unwilling others.

> The typical politician is not only a rascal but also a jackass, so he greatly values the puerile notoriety and adulation that sensible men try to avoid. (*The Impossible Mencken*, p. 66)

There's nothing like telling the crowd not only that the emperor is stark naked, but that he's ugly to boot. One of our great political myths is that politicians are public servants—men and women who seek office "to change the world" or "to serve their country"—people whose public statements reveal their private, noble sentiments—officials with supernatural powers to care about each of us and to sacrifice for us in ways that would shame our mothers.

The reality, as Mencken understood, is that people seek public office generally for the same reason that people want to be movie stars or rock idols. They want their faces to be recognized; they want to be applauded as Very Important People: and they want to feel superior to the millions of people who are never interviewed on television, quoted in the *New York Times*, or feted by the rich and the famous. They want to get seated without reservations at the most exclusive restaurants.

These desires are natural. Anyone who reflects honestly on himself will see that he, too, gets a thrill from the thought of possessing fame and its accompanying perks. But as Mencken says, sensible men nevertheless try to avoid such fame, for this desire is juvenile. Its pursuit—and, much more, its possession—distracts people from such genuinely worthwhile goals as being an attentive parent and friend, being honest, and being productive.

> It is the theory of all modern civilized governments that they protect and foster the liberty of the citizen; it is the practice of all of them to limit its exercise, and sometimes very narrowly. (*The Impossible Mencken*, p. 74)

Says it all.

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The Greenspan Fed in Perspective

ROGER W. GARRISON

On average, Federal Reserve chairmen come and go at about the same rate as U.S. presidents. Dating from the creation of this country's central bank (1913), we have seen 16 presidents (Wilson to Bush) and 14 Fed chairmen (Hamlin to Bernanke). The Fed chairmanship, however, has seen more variation in years of service—Franklin D. Roosevelt notwithstanding. Spanning four presidencies, Alan Greenspan's reign (1987–2006) was the second longest. Greenspan was outdistanced (but only by a few months) by William McChesney Martin (1951–1970), who served five presidents.

The first half-dozen Fed chairmen belong to a different era—during which the primary locus of control on policy matters was the New York Federal Reserve Bank. It was that bank's Benjamin Strong and, following him, George Harrison who were key operatives during the late 1920s' expansion and the subsequent crash and descent into deep depression. And it was just as the economy was bottoming out that Congress passed legislation (in 1933 and 1935) that, among other things, shifted power to Washington. Though there is no Federal Reserve Bank in the nation's capital, the Eccles Building on Constitution Avenue, built in 1937 and now named for the seventh Fed chairman, houses the Board of Governors and, most importantly, the chairman of the Board.

> Key to understanding these open-market operations, as they are called, is the fact that, unlike ordinary purchasers of treasury bills, the Federal Reserve buys treasury bills with funds that were not in existence before it made the purchase. It spends new money into existence.

Like Marriner Eccles, the early and middle Fed chairmen were not economists. Instead, they had backgrounds in law, banking, or finance. But starting with Arthur Burns (1970–1978) and allowing for one short gap of 17 months, an economist has been at the top of this country's banking pyramid. A nearly unbroken reign of economist-chairmen—Burns, Volcker, Greenspan, and now Bernanke—has characterized modern Fed history. Having an economist at the top does not necessarily translate into better policy, but it does make the policy regime more understandable in terms of economic theory.

The one short gap—between the Keynesian-oriented Burns and the monetarist-oriented Volcker—was bridged by the unlikely G. William Miller (March 1978–August 1979). Appointed by President Carter and somehow confirmed by the Senate, Miller was a marine engineer turned lawyer. He was a long-time executive of Textron, Inc., and, on several occasions, had served the Carter administration in an advisory capacity. Clearly out of his element, Miller oversaw the acceleration phase of that period's double-digit inflation. Following established procedure for managing total bank reserves and

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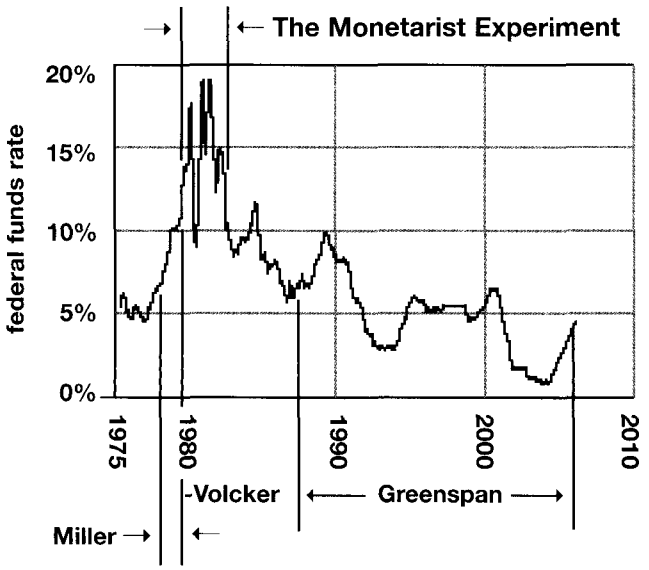
hence deposit money, Miller and the other members of the Board (plus some Reserve Bank presidents) met about every month and a half to set short-term interest rates. They literally "set" the discount rate, the rate at which the Fed lends reserves directly to commercial banks, and they "targeted" (about which more below) the federal funds rate, the overnight rate at which commercial banks lend to one another for the purpose of meeting their reserve requirements, those requirements themselves having been imposed by the Fed.

During the 17 months of Miller's tenure the discount rate was increased from 6½ to 10¼ percent, the fed-funds target rate from 6¾ to 11 percent. Though responding to political pressures to keep interest rates low, the Miller Fed was constrained in each policy meeting by the inflation that had resulted from decisions in earlier meetings. With prices and wages rising at double-digit rates by the end of the decade, the Fed-controlled interest rates (both set and targeted) continued to rise in nominal terms, but were actually near zero or even negative in real terms. And as was well understood in financial and academic circles, holding nominal rates of interest below the inflation rate is a policy that cannot be sustained.

Finally, to stop the bleeding and to appease fiscal conservatives, Carter moved the chairman from the Federal Reserve to his own cabinet—where, as secretary of the treasury, Miller could borrow lots of money but couldn't create any. Paul Volcker, then president of the New York Fed, was brought in as the new chairman of the Board. The circumstances under which Volcker assumed



the chairmanship were unique and significant: (1) interest-rate targeting as a means of limiting inflation had lost its credibility. (2) Milton Friedman's monetarism, which focused attention on the growth rate of the money supply rather than on short-term interest rates, was gaining acceptance in academic circles and beyond. And (3) the new Fed chairman had the support of fiscal conservatives both in Washington and on Wall Street.

In early October 1979, the Federal Reserve switched its modus operandi from fed-funds targeting to money-growth targeting. It never quite adopted Friedman's monetary rule—according to which it should increase the money supply at a constant and pre-announced low-single-digit rate. But deliberations at the policy meetings were conducted in terms of money-growth rates rather than fed-funds rates. The money-growth rate and hence the inflation rate were brought down, while the fed-funds rate found its own level at record highs—topping out twice at 19 percent in 1981 and not returning to pre-Miller levels for several years.

As an episode in money-growth targeting, the so-called monetarist experiment lasted only three years (1979–1982). The key monetary aggregate, christened M1, was made up of coins, currency, and checking-account balances. M1 provided a solid anchor for money-growth policy at the beginning of the experiment, but the experiment itself led to a complete unanchoring of monetarism at the end. The story involves a heavy dose of monetarist irony.

The 1930s' banking reforms that restricted policymaking to Washington also restricted the behavior of banks in critical ways. A Federal Reserve statute (Regulation Q) imposed key restrictions on demand deposits and time deposits. In effect, depositors were precluded from having a single account on which they could (1) write checks and (2) earn interest. The statute also set strict limits on savings-account interest rates. Though not implemented with money-growth targeting in mind, Regulation Q gave rise to a sharp distinction between money (that is, checkable accounts) and savings (that is, interest-earning accounts). This either-or aspect of money and savings allowed for a crisp definition of *the* money supply. M1 was money that people could actually *spend* and hence was unquestionably the basis for policymaking. The larger monetary aggregates (M2, M3,

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and still-more-encompassing M's) included heavier and heavier doses of savings and thus were not so relevant to the issue of inflation.

And herein lies the monetarist irony. According to this free-market school of thought, the Federal Reserve can keep the economy performing at its laissez-faire best by ignoring interest rates and focusing instead on *the* money supply. But having a money-supply magnitude worthy of the Fed's attention required this one critical departure from laissez faire called Regulation Q. Compounding the irony was the effect of the monetarist experiment on the viability of Regulation Q. As long as market interest rates hovered in the low single digits, the distortions caused by interest-rate ceilings (including a ceiling of zero percent on checkable accounts) were relatively minor. But the Miller Fed and subsequent monetarist experiment produced market rates of interest in excess of 20 percent, creating strong incentives for the banking industry to circumvent Regulation Q. The circumvention started with NOW accounts (Negotiable Order of Withdrawal), which were, in all but name, checkable savings accounts. Soon after, money-market mutual funds arose to help savers take advantage of the high treasury-bill rates. These and other such financial innovations threatened the very existence of commercial-bank savings accounts. The legislative reaction was bank deregulation, initiated during the Carter administration and accelerated in the early years of the Reagan administration. By 1982 Regulation Q was gone—and so too was the crisp distinction between checking accounts and savings accounts and the special significance of M1.

Though the Volcker Fed persistently missed its money-growth targets on the high side, it could claim to have done fairly well in dealing with inflation, at least in comparison to the Miller Fed. But in setting relatively low money-growth targets, it had destroyed (through high interest rates and bank deregulation) its ability even to identify a relevant money-supply magnitude. In 1982 the Volcker Fed reverted to targeting the fed-funds rate, not really by choice but because that was the only target left standing.

> Some readers of the *WSJ* might have been led to believe that Greenspan had somehow followed Friedman's monetary rule. We now see, though, that there was no well-grounded rule; there was no standard.

The Greenspan Era

When Alan Greenspan became Fed chairman on August 11, 1987, the interest-rate targeting continued. There was early and continued criticism of Greenspan because of his focus on interest rates rather than on monetary aggregates. As Bob Woodward reports in *Maestro: Greenspan's Fed and the American Boom* (2000), the notion of money-supply targeting was still alive in 1989 in the person of Richard Darman, President George H. W. Bush's budget director. Darman complained that Greenspan was mismanaging the money supply and, in particular, that the money-growth rate was too low. Greenspan responded dismissively with the claim that Darman had some sadly out-of-date notions. Without actually explaining to his readers just why those monetarist notions were out of date, Woodward remarked, "The Fed couldn't even measure the money supply accurately, let alone control it" (p. 63).

As was true before the short period of money-supply targeting, the only interest rate that the Federal Reserve could actually get in its crosshairs was the fed-funds rate. That rate comes highly recommended as a target if the only criterion is the answer to the question "Can the Fed actually aim at—and hit—the target?" The answer is yes. The Fed can add to (or subtract from) bank reserves by buying (or selling) treasury bills. When the trading desk at the New York Fed buys a treasury bill from a commercial bank, the bank's earning assets are reduced by the value of the treasury bill and its reserves (funds not lent out) are increased by that same amount. (Key to understanding these open-market operations, as they are called, is the fact that, unlike ordinary purchasers of treasury bills, the Federal Reserve buys treasury bills with funds that were not in existence before it

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made the purchase. It spends new money into existence.) And because the fed-funds rate is the rate that governs interbank transactions made on an overnight basis (as banks with excess reserves lend to banks with reserve deficiencies), the impact of increased reserves on the fed-funds rate is immediate. The timely feedback observed by the Fed's trading desk allows it to adjust the volume of treasury bills bought or sold so as to achieve the targeted fed-funds rate. The Federal Reserve is never very far off target on any given day. On the basis of weekly averages, the Fed's aim looks even better, and on the basis of monthly averages, the Fed scores a bull's-eye every time.

Hitting the chosen fed-funds rate is not a problem. But choosing the particular fed-funds rate to target is another matter. Some choices are clearly non-viable, as was roundly demonstrated by the Miller Fed. Targeting too low a fed-funds rate requires a large infusion of reserves, which gives rise to a dramatically increasing money supply, which causes substantial inflation, which puts an inflation premium on all interest rates, which precludes the Fed's having such a low target rate. The Miller Fed persistently failed to raise its target rate enough to keep up with the rising inflation premium.

Targeting too high a fed-funds rate might require a shrinkage of reserves, which would force a monetary contraction and put the economy into recession, weakening the business community's demands for loans and hence reducing market rates of interest. The targeted fed-funds rate that was already too high is thrown even further out of line with actual market conditions.

Unfortunately for central banking, there is a wide spectrum of potential fed-funds target rates between clearly too low and clearly too high. Here, the root problem faced by the Fed is no different from the problem associated with a more general central control of economic activity. The Food Czar of a command economy can easily conceive of too many chickens or too few chickens. But the Goldilocks number of chickens—like the Goldilocks fed-funds target rate—doesn't identify itself. Of course, in a thoroughly decentralized economy, it is the market-determined price of chickens—and the market-determined interest rates—that keep the economy functioning smoothly.

In choosing a fed-funds target rate, Greenspan's thinking—at least early in his reign as Fed chairman—seemed to acknowledge the significance of having a rate that was just right. Referring to a 1989 episode, Woodward accurately captures Greenspan's view: "[T]he Fed's interest-rate policy had to be credible. A particular fed-funds rate had to be seen by markets as the best rate for the economy, not as an artificially low rate influenced by political pressure" (p. 62). Here, we see not only a bow to the market economy but a teasing hint at the Mises-Hayek theory of the business cycle: Holding interest rates artificially low sets the economy off on an unsustainable growth path. The policy-induced boom eventually ends in a bust. To avoid boom and bust, resources had to be allocated on the basis of the "natural rate of interest," so named by Swedish economist Knut Wicksell and adopted as the market benchmark by Mises and Hayek.

Unfortunately, the very existence of a central bank precludes its knowing what the natural rate of interest is. That rate is the rate that would prevail "naturally," that is, as the result of the give and take of decentralized forces in the absence of a central bank. Whatever theoretical understanding Greenspan retained from his early studies in Austrian economics, his practical approach to managing the monetary system was very conventional: raise the fed-funds target to counter inflationary pressures; lower the fed-funds target to counter unemployment.

Too High for Politics

While keeping with convention, interest rates were kept too high for George H. W. Bush's political purposes in the 1992 presidential campaign. That was the claim made by the Republican leadership—and the reason for the widely perceived bad blood between Bush and Greenspan. But Greenspan was not always blind to political objectives. He signed on as a team player early in the Clinton administration and played a strong supporting role in Clinton's 1996 campaign. Clearly (in retrospect and even at the time) the Fed's lowering of the fed-funds target rate early in that election year was intended to counter the Republican Party rather than to counter unemployment.

While departing from the principles of central bank-

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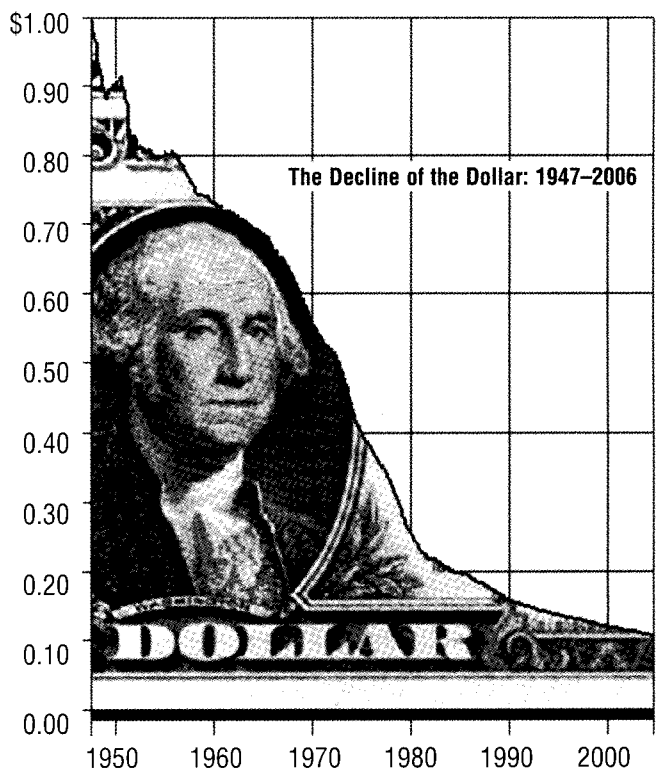
ing to give the Clinton campaign an edge, Greenspan departed from his Austrian roots in explaining the mid-to-late-1990s boom. He articulated a theory—or, at least, a belief—that ran completely counter to the Austrian theory. As reported by Woodward (pp. 171ff.), Greenspan persistently held to the belief—though a belief without proof—that productivity had increased on an economywide basis, creating what was popularly called the "New Economy." Higher productivity would mean increasing output, which would hold price and wage inflation in check even as the Fed pursued an easy-money policy.

Greenspan's calculations, however, are especially revealing. Inexplicably, he made his estimates of the supposed increase in productivity on the basis of the assumption that non-labor costs are constant. Surely, though, this is a peculiar assumption for the Fed chairman to make in light of the fact that non-labor costs include the cost of borrowing, which are affected rather dramatically by Fed policy. Lower borrowing costs—a.k.a. artificially low rates of interest—get reflected in increased profits for a wide variety of business firms. If non-labor costs are (counter to fact) assumed to be constant, then those increased profits will be mistakenly seen as evidence of a general increase in labor productivity. But since productivity gains are rarely across-the-board gains, it is much more likely that what Greenspan was observing was not some New Economy at all but rather the Old Economy goosed up by credit expansion.

In any case, the economywide downturn that began in late 2000 put an end to both the Clinton-Greenspan expansion and the so-called New Economy. Perhaps the only thing new about that period was the increasing irrelevance of the monetary aggregates. As already indicated, the once-all-important M1 had lost much of its significance with the 1980s monetary deregulation and in particular with the phasing out of Regulation Q. But during the increased globalization of the 1990s, this one-time key monetary magnitude lost virtually all its significance. As M1 actually declined from the mid-1990s through the turn of the century, its currency component rose dramatically. The ratio C/M1 rose from well below 30 percent at the beginning of the Greenspan years to well over 50 percent at the end—with most of that increase occurring during the last half of the 1990s. The dramatic change reflected not the increased use of currency in the United States but the increased use of U.S. currency outside our borders. Stashes of dollars in unstable Middle Eastern countries as well as the widespread circulation of dollars in former Soviet-bloc countries and in Latin American countries that have become (officially or unofficially) dollarized help account for the high demand of U.S. currency.

Friedman's monetarism and especially his monetary rule, as articulated with the aid of the bedrock equation of exchange ($MV = PQ$), requires that the M and the P and the Q all refer to the same piece of geography. It just won't do, for instance, to take P and Q to be the U.S. Consumer Price Index and the U.S. Gross Domestic Product and to take the corresponding M to be M1—much of which is outside the United States. But the Federal Reserve has no way of tabulating $M1_{US}$. That is, Greenspan knew how much M1 had been created, but he didn't know where in the world it was. Trying to manage the money supply directly, then, that is, adopting a policy of money-supply targeting, was increasingly problematic. More so than ever, fed-funds targeting was all there was to do.



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"Neutral Interest Rate"

Fed watchers during the last years of Greenspan's chairmanship have repeatedly encountered the term "*neutral* rate of interest" in discussions of the Fed's choice of fed-funds target rates. That term could be taken as evidence that Greenspan had returned to his Austrian roots and wanted to target a fed-funds rate consistent with the "*natural* rate of interest," that is, the rate of interest that would prevail in a market unhampered by a central bank. But "Greenspan-neutral" is not the same thing as "Austrian-natural." The Fed knows that if it sets interest rates too low, there will be worries about inflation, and if it sets interest rates too high, there will be worries about unemployment. The goal, then, is to balance the worries—that is, to find the equi-worry fed-funds rate. That's what's meant by the neutral rate.

But just whose worries count? The worries emanating from financial markets? Traders in financial markets might worry about interest rates being too low or too high—but mainly because of the implications about future actions by the Federal Reserve. Is the Fed going to raise rates? Is it going to lower them? The neutral fed-funds rate, then, would be the rate that causes the financial markets to have no net worry about the fed-funds rate changing in one direction or the other. If *this* is the balancing act that underlies Federal Reserve policy, then both the Fed and financial markets are living in a house of mirrors.

Is there any known market mechanism that causes the neutral rate to be brought into line with the natural rate? That is, is there any reason to believe that equi-worry about inflation and unemployment translates into interest rates that are consistent with sustainable growth? Or is it quite possible that the Greenspan-neutral rate lies below the Austrian-natural rate? We have the answer to this question from Greenspan himself—as summarized by Woodward: "There was no rational way to determine that you were in a bubble when you were in it. The bubble was perceived only after it burst . . ." (p. 217). Evidently, the equi-worry rate itself is something to worry about.

On the last day that Alan Greenspan served as Fed chairman, Milton Friedman penned a commentary in the *Wall Street Journal* (January 31, 2006) titled "He Has Set a Standard." Some readers of the *WSJ* might have been led to believe that Greenspan had somehow followed Friedman's monetary rule. We now see, though, that there was no well-grounded rule; there was no standard. In truth, Greenspan pitted worry against worry and was lucky enough to make it to the end of his final term despite there being no standard at all.

And now, Ben Bernanke has pledged to continue the policies of the Greenspan Fed—possibly with a little less worry about inflation. We can only wonder how long his luck will hold out.

> The abandonment of the gold standard made it possible for welfare statists *to use the banking system* as a means to an unlimited credit expansion. . . . In the absence of the gold standard, there is no way to protect savings from confiscation through inflation.
>
> —Alan Greenspan, "Gold and Economic Freedom," 1966

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Institutions and Development: The Case of China

BY JAMES A. DORN

From a liberal perspective the goal of economic development is not simply to maximize output but, rather, to increase freedom of choice. As Peter (Lord) Bauer wrote in *Economic Analysis and Policy in Underdeveloped Countries*, "I regard the extension of the range of choice, that is, an increase in the range of effective alternatives open to people, as the principal objective and criterion of economic development." Those countries that have liberalized trade—such as China and South Korea—have expanded individual choices and outperformed those that have clung to protectionism—such as Cuba and North Korea.

When considering how individuals and nations move from poverty to prosperity, one needs to emphasize that natural constraints (scarcity of resources) can be overcome if artificial constraints (such as trade restrictions) don't impede development. This idea is consistent with Hong Kong Chief Executive Donald Tsang's call for adherence to the principle of "small government, big market."

There is a saying in China: "If no artificial constraints, then there is nothing you cannot do." Nonintervention (*wu wei*) results in spontaneous order (*zi fa*) if government is limited to the protection of persons and property. In the fourth century B.C., long before Adam Smith, the great Chinese philosopher Lao Tzu held that when the ruler takes "no action," "the people of themselves . . . become prosperous."

In the fourth century B.C., long before Adam Smith, the great Chinese philosopher Lao Tzu held that when the ruler takes "no action," "the people of themselves . . . become prosperous."

Wu wei does not imply "the complete absence of all activity, but only of such as is forced, artificial, and unspontaneous," according to Derk Bodde, the translator of Fung Yu-lan's classic *A History of Chinese Philosophy*.

The Taoists saw a good government as one consistent with nonintervention so people could improve their welfare. Thus in the *Chuang-tzu*, we read: "Where knowledge and plans are not utilized, one must fall back upon the natural. This is perfect peace, the acme of good government."

In the *Han Fei Tzu* (Han Fei was a legalist who died in 233 B.C.), one sees a clear understanding of the importance of free trade for creating harmony and prosperity:

> When a man sells his services as a farm hand, the master will give him good food at the expense of his own family, and pay him money and cloth. This is not because he loves the farm hand, but he says, "In this way, his ploughing of the ground will go deeper and his sowing of seeds will be more active." The farm hand, on the other hand, exerts all his strength and works busily at tilling and weeding. He exerts all his skill cultivating the fields. This is not because he loves his master, but he says: "In this way I shall have good

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> soup, and money and cloth will come easily." Thus he expends his strength as if between them there were a bond of love such as that of father and son. Yet their hearts are centered on utility, and they both harbor the idea of serving themselves. Therefore in the conduct of human affairs, if one has a mind to do benefit, it will be easy to remain harmonious, even with a native of Yüeh [a barbarian state]. But if one has a mind to do harm, even father and son will become separated and feel enmity toward one another.

This passage was written more than 2,000 years before *The Wealth of Nations*!

In 1987 China's paramount leader and reformer Deng Xiaoping recognized the principle of spontaneous order when he said: "Our greatest success—and it is one we had by no means anticipated—has been the emergence of a large number of enterprises run by villages and townships. They were like a new force that just came into being spontaneously."

Kate Xiao Zhou, in her 1996 book *How the Farmers Changed China*, describes the demise of China's collective farms and the creation of the household-responsibility system (*baochan daohu*), with its township and village enterprises (TVEs), as "a spontaneous, unorganized, leaderless, nonideological, apolitical movement."

China began to unilaterally liberalize foreign trade well before joining the World Trade Organization in December 2001. The first four special economic zones (SEZs) were created in 1980, and since then the coastal provinces (such as Guangdong, Zhejiang, and Fujian) have become highly "marketized." The nonstate sector, including private firms, now overshadows the state sector.

Nicholas Lardy, a China specialist at the Institute for International Economics, has pointed out that in 1978 only 12 large state-owned enterprises (SOEs) were authorized to conduct foreign trade. However, by 2001 there were 35,000 domestic firms engaged in international trade, including private enterprises, and more than 150,000 foreign-funded enterprises. Today any registered firm can engage in foreign trade. Moreover, China reduced the average tariff rate from 55.6 percent in 1982 to 15.3 percent at the beginning of 2001. The average tariff on manufactured goods is now less than 9 percent. As a result of this dramatic liberalization, China is now one of the world's most open economies.

China's approach to development has been primarily "bottom-up," or experimental. Typically, local leaders would permit reform on a trial basis and not penalize entrepreneurs who were experimenting on their own. When successful, politicians would take credit and let the experiment spread. At some point Beijing would sanction the reforms.

China's approach to development has been primarily "bottom-up" or experimental. Typically, local leaders would permit reform on a trial basis and not penalize entrepreneurs who were experimenting on their own.

Piecemeal reform has led to numerous ownership forms, including cooperative shareholding, foreign-funded enterprises, private firms, and TVEs. Economists Gary Jefferson and Thomas Rawski call this process "induced privatization." Under it the state sector has shrunk from a dominant position in 1978 to less than one-third of industrial output value today.

Property Far from Secure

By letting the nonstate sector grow, China has avoided the difficult political decision of outright privatization of large SOEs. Private firms were not legal until 1988, and in 2004 the PRC constitution was amended to give greater protection to the growing private sector. Private property rights, however, are still far from secure, and corruption is rampant. So while economic liberalization has progressed, and China has become the world's third-largest trading nation, the Chinese Communist Party (CCP) retains its monopoly on power.

Nevertheless, China's opening to the outside world has increased personal freedom and prosperity, and has led to a demand for safeguarding private property rights. Jianying Zha, in her fascinating book *China Pop*, writes, "The economic reforms have created new opportunities, new dreams, and to some extent, a new atmosphere

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and new mindsets. . . . There is a growing sense of increased space for personal freedom."

Kathy Chen of the *Wall Street Journal* notes that the development model adopted by the newly emerging urban centers, such as Shishi in Fujian, is "small government, big society" (*xiao zhen fu, da she hui*).

When the National People's Congress amended the constitution to make "legally acquired private property *inviolable*," that was a clear signal the market was here to stay—and a far cry from Mao Zedong's admonition to "strike hard against the slightest sign of private ownership."

There is no doubt that globalization and the information revolution have increased personal freedom in China. More than 100 million Chinese have access to the Internet.

And I am sure that computer whiz-kids will stay one step ahead of government censors. Moreover, if Shanghai is to become a world-class financial center, there will have to be a freer flow of information and open capital markets.

President Hu Jintao has recently indicated his adherence to a policy of "peaceful development," which is precisely the policy that China has been following since 1978. The United States would be wise to continue a policy of engagement and avoid destructive protectionism. Foreign-funded enterprises and private firms account for more than 60 percent of China's foreign-trade sector. U.S. protectionism would harm the very sector that is working to decrease poverty, increase exposure to the West, and pressure the CCP to accept change.

Institutional reform (especially trade liberalization) has substantially reduced poverty in China—real per capita income has increased nearly fivefold since 1978, with significantly larger increases in the highly marketized coastal areas. But there has been little increase in political freedom. Further economic liberalization—especially privatization of large SOEs and capital freedom—is constrained by political issues. Whether reformers in the CCP will gain the upper hand remains to be seen.

An array of government interventions continues to restrict economic and personal freedom, and, hence, China's future development. Artificial constraints include capital and exchange controls, state-owned banks and enterprises, interest-rate controls, and especially the lack of a transparent legal structure that protects persons and property.

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"Free Private Markets"

In 1988, at the Cato Institute's historic conference in Shanghai, Milton Friedman called for China to abandon its socialist market economy and make the transition to a full-fledged system of "free private markets." Progress has been made since that time, as markets not planners determine most prices. There is private housing and private enterprise, but China is still plagued by widespread state ownership and control, especially in the financial sector. Without capital freedom, investment alternatives will be limited and investment decisions will continue to be politicized.

Privatization is the only way to rid the system of corruption. But as long as the CCP gains from the present socialist market system, change will proceed slowly, if at all. Economic reform eventually will require political reform. The question is whether the gradual increase in economic freedom will be sufficient to bring about political change that supports, rather than retards, further liberalization.

We should not forget that trade expands choice and, therefore, should be promoted as a fundamental human right. U.S. protectionism would be self-defeating and strengthen Chinese nationalism and anti-American sentiments. Engagement is the only rational policy to promote peace and prosperity.

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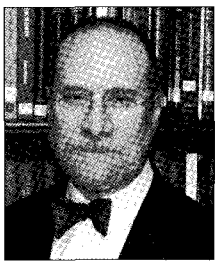
"The Tariff Is the Mother of Trusts"



BY SHELDON RICHMAN

In articles such as Roy Childs's "Big Business and the Rise of American Statism," Murray Rothbard's "War Collectivism in World War I," and Joseph Stromberg's "The Role of State Monopoly Capitalism in the American Empire," advocates of the freedom philosophy have laid the blame for big government largely at the door of business. This may conflict with the way we'd expect things to be, but ultimately this is a historical matter to be settled empirically.

Besides, why should we expect business people to favor laissez faire and to abhor government intervention? Few people outside of business do so. Why would people in business be different? As Albert Jay Nock noted long ago, people tend to favor the path of least exertion. If a business owner can increase his profits with a tax, regulation, or import quota on his domestic or foreign competitors, why not go for it? You and I may expect his ethical governor to stop him. But what if he, like most other people, doesn't equate government action with plunder? In that case he won't see himself as a hooligan once removed. Rather, he'll see himself as a citizen in a democracy petitioning his government for badly needed relief, which, as it happens, will also serve the general welfare.

Why should we expect business people to favor laissez faire and to abhor government intervention? Few people outside of business do so.

There's another consideration. You and I know that the business cycle is a creation of central banking. Panics, depressions, and recessions are not found in the pure market economy. They are the result of manipulation of money by a political authority. But most people don't know that. Business people throughout U.S. history have believed that the trade cycle is inherent in nature, and they looked to government to moderate if not eliminate it. If business people were familiar with Mises and Hayek's trade-cycle theory, big-business statism might be harder to understand. As it is, there is little mystery at all.

The above-mentioned writers go one more step and connect interventionism at home with interventionism abroad, that is, imperialism in one form or another. This should come as no shock. Those who want government to manage the national economy for the betterment of "the nation" (or at least their firms and industries) will easily believe that it should manage the world economy for an even greater good. American nationalism almost from the beginning lent itself to the messianic view that only the United States could bring enlightenment to the rest of the world—and at a profit to boot.

Why should manifest destiny have been restricted to the continent? In 1898 it was extended to the Philippines, with the shedding of much blood and the death of self-determination. (Laissez-faire advocates like William Graham Sumner and Edward Atkinson objected.)

That some enemies of markets (Lenin, for example) also saw a connection between business and imperialism doesn't mean no connection exists. States regulate economies, and states make war, conquer territory, and impose their influence. The common element is obvious.

Ludwig von Mises in several places makes the connection between domestic and foreign interventionism. "A nation's policy forms an integral whole. Foreign policy and domestic policy are closely linked together; they are but one system; they condition each other," Mises wrote in *Omnipotent Government*. "Where there is free trade, foreign competition would even in the short run

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frustrate the aims sought by the various measures of government intervention with domestic business. When the domestic market is not to some extent insulated from foreign markets, there can be no question of government control. The further a nation goes on the road toward public regulation and regimentation, the more it is pushed toward economic isolation."

Regulation increases the cost of doing business, giving an advantage to foreign competitors, who therefore must be denied free access to the home market. Under the right circumstances, burgeoning protectionism, the breakdown of the division of labor, and the need for raw materials instill thoughts of war and conquest in ambitious national leaders.

Moreover, protectionism, by excluding low-cost competition, has a cartelizing effect on domestic industry. "The tariff is the mother of trusts" they used to say. This means that artificially fewer firms can charge higher prices and pay lower wages than would have been the case in a fully competitive market. In reality the welfare of "the nation" is paid for dearly by consumer-workers. As Cobden and Bright knew, laissez faire is the workingman's cause.

Cartelization sets the stage for the next round of intervention. As Joseph Schumpeter, an economist friendly to the market economy (if pessimistic about its prospects), explained in *Imperialism and Social Classes*, at the high prices induced by protectionism, firms can't sell enough units to take advantage of economies of scale. "The trust thus faces a dilemma," Schumpeter wrote. "Either it renounces the monopolistic policies that motivated its founding; or it fails to exploit and expand its plant, with resultant high costs. It extricates itself from this dilemma by producing the full output that is economically feasible, thus securing low costs, and offering in the protected domestic market only the quantity corresponding to the monopoly price—insofar as the tariff permits; while the rest is sold, or 'dumped,' abroad at a lower price, sometimes (but not necessarily) *below* costs."

Thus "overproduction" is now a new problem for the government to solve. How? By securing foreign markets in which the surpluses can be unloaded. "Securing foreign markets" is a mandate bursting with potential for state mischief, which is to say bullying and war.

Say's Law

You and I know, as J.B. Say taught, that there can be no general overproduction in a free economy, but we're not talking about free economies and people familiar with Say's Law. We're talking about an interventionist environment in which business people have unsold surpluses on their hands. Who are they gonna call? Not Ghostbusters. The result is the Open Door policy, gunboat diplomacy, and a world fiat-monetary system, punctuated by the occasional shooting war.

Schumpeter goes on: "Thus we have here, within a social group that carries great political weight, a strong, undeniable economic interest in such things as protective tariffs, cartels, monopoly prices, forced exports (dumping), an aggressive economic policy, an aggressive foreign policy generally, and war, including wars of expansion with a typically imperialist character. Once this alignment of interests exists, an even stronger interest in a somewhat differently motivated expansion must be added, namely, an interest in the conquest of lands producing raw materials and foodstuffs, with a view to facilitating self-sufficient warfare." I would only add that the conquest can be political rather than military.

As Stromberg points out, things need not occur in the exact order in which they did in the past. Under other circumstances, effects can be causes. The point is that tampering with the market economy creates its own justification for more tampering, and on and on. When a state's tampering achieves global dimensions, we have empire, or something with a strong resemblance. That the script is often scored with a seemingly pro-market soundtrack ("globalization" and "free trade") changes no facts. It may be "capitalism" (I'll leave that issue for another day), but it's surely not the free market.

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Leviathan's Legionnaires

BY BECKY AKERS

Boston lies under a foot of snow this Monday March evening in 1770, so icy and cold that anyone who can huddle at home on the hearth should. Instead, much of the town is abroad and abuzz like an angry hive. Bostonians are infuriated at something their descendants will take for granted, indeed, will prize so highly they'll pay for it: police are patrolling their city.

And have been for many months. In September 1768 a thousand British Redcoats disembarked at the town's wharves. From there they "marched sword in hand through the principal streets of [Boston], then in profound peace."[1] Their purpose was not to protect the 15,000 inhabitants but to keep them in line, much as police presently do. And, again like modern officers, they will collect money for the government, though rather than writing traffic tickets, they will enforce customs duties.

Boston Massacre

The colonists do not share their descendants' idealism that the police "protect and serve," nor do they mistake the Redcoats for "Boston's Finest." They see the soldiers stalking among them as the government's bullyboys, and they despise them for it. Tonight, that antagonism will explode, becoming famous as a Massacre for killing five civilians and wounding others.

Historians offer a bevy of explanations and excuses for that calamitous confrontation: Americans resented the British as an occupying force; off-duty soldiers worked at odd jobs for low pay, stealing opportunities from Boston's day laborers and provoking more resentment; the Redcoats were naturally arrogant, the colonists naturally touchy. But behind it all lies the simple fact that the soldiers were policing Boston. They marched through the city searching for contraband, infractions of the government's rules, and anyone the administration deemed suspicious.

They also reintroduced His Majesty's customs officers at the point of their bayonets. Prior to the Redcoats' advent in 1768, Bostonians had so intimidated these officials that they fled the city. Ann Hulton was sister to one; she wrote, "Every officer of the Crown that does his duty is become obnoxious & they must either fly or be sacrificed. . . ." Ann flew with her brother and others to Castle Island, now part of the mainland but then a fort lying at a safe distance in Boston Harbor. From there, Miss Hulton continued her account of the colonists' cowing of Customs: "These Sons of Violence after attacking Houses, breaking Windows, beating, Stoning & bruizing several gentlemen belong'g to the Customs, the Collector mortally & burning his boat."[2] Only when the Redcoats could ensure their safety did the officers return to Boston. They remained for the next 18 months, retreating again with the troops after the Massacre: "The inhabitants of the town assembled in Faneuil Hall . . . unanimously resolved, that no armed force should be

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suffered longer to reside in the capital . . . . [T]he people, inflexible in their demands, insisted that not one British soldier should be left within the town . . . . [W]ithin four days the whole army decamped. . . . The commissioners of the customs and several other obnoxious characters retired with the army" to the fortified Castle Island.[3]

Could we whisk the army from their eighteenth-century fort to a modern precinct, the Redcoats would likely agree that their policing differed little from today's—except in one remarkable detail. They would be astounded at the enormous authority most Americans grant the police and at the enormous respect, even glorification, following from that.

Both are centuries removed from the ridicule and revulsion red-coated police rated in eighteenth-century Boston. Perhaps the difference in attitude arises partly from our powerlessness against a force armed far beyond what most of us can manage. The Bostonians milling about the freezing streets that night carried pistols and swords every bit the equal of muskets and bayonets. If a man didn't own a gun or blade, he hastened toward the coming showdown with the "invaders" and "foreign enemies" openly bearing a wooden stave or club, a knife, a hatchet, even a chunk of ice scooped off the street.[4]

Their weapons rendered the colonists boisterous and aggressive when standing up to the Redcoats. British General Thomas Gage reported that "The people were as Lawless and Licentious after the Troops arrived, as they were before. The Troops . . . seemed only offered to abuse and Ruin . . . to suffer ill usage and even assaults upon their Persons till their Lives were in Danger. . . ."[5]

That "lawlessness" bedeviled the Redcoats from their first moments in Boston, when they began hunting barracks. Thomas Hutchinson, Massachusetts's royally appointed governor, offered a large public building to the soldiers, ignoring the "outcasts of the Workhouse and the scum of the Town"[6] already renting rooms there. The "scum" objected to the governor's exercise of eminent domain as much as Hutchinson would have had they offered the Redcoats his mansion. They promptly barricaded themselves inside the building.

Boston's sheriff, backed by some soldiers, soon arrived. He discovered an unlocked window, climbed into the building, and ordered the "outcasts" out. They promptly barricaded him inside, too.

Meanwhile, the sheriff's martial escort stood helpless, unable to rescue him, because the scowling, muttering townspeople surrounding the place heavily outnumbered the soldiers. This standoff continued for two days after Boston's Council sided with the "scum" and refused to authorize their eviction.

Nor did the colonists' "ill usage" abate over the next year and a half. Before the shooting began on the night of the Massacre a citizen scolded a group of British officers: "Why don't you keep your soldiers in the barracks? . . . Are the inhabitants to be knocked down in the streets? Are they to be murdered in this manner? You know the country has been used ill. You know the town has been used ill. We did not send for you. We will not have you here."[7]

Contrast that succinct and spirited lesson in liberty with the shuffling slave mentality of modern Americans. We bow and scrape when dealing with police officers in their various guises, whether the state trooper during a traffic stop or the Transportation Security Administration screener searching us without cause or warrant at the airport.

Also astonishing is the deference the Redcoats' officers showed the colonists. Sometime after one Bostonian had scolded the officers, another asked British Captain John Preston whether he would order his men to fire on them. "By no means, by no means," Preston answered respectfully. "My giving the word 'fire' under those circumstances would prove me no officer."[8] Thus while modern police order us about as though we are slow and stupid children, British officers requested, explained, and begged pardon.

After the Redcoats fired that night, a silversmith named Benjamin Burdick approached, obviously studying the troops in the moonlight. "I want to see some faces that I may swear to another day," he said. Would any of us dare stop when we see a car on the side of the highway, with a trooper ticketing the driver, to announce ourselves as witnesses? Granted, Burdick was an imposing man, estimated to weigh 380 pounds by a neighbor,[9] but even the largest among us is unlikely to heckle an armed cop. Not only do they outgun us, but there are too many laws protecting them, too much presupposition that, in any encounter, the state is right and the citizen wrong. The Redcoats in eighteenth-century

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Boston could rely on no such privileges. Indeed, the only response Captain Preston made to the brave Burdick was a mild, "Perhaps, sir, you may [be summoned to court as a witness]."[10]

Unthinkable, isn't it? The police buffaloed, and citizens riding herd on them! But that's become an impossible dream; it is as if the people and the police have swapped places. Why? Are Americans really that different now? Or have policemen, their nature and their relationship to the people they "serve," changed?

William the Conqueror

Eighteenth-century Englishmen, whether in the colonies or at home, had a horror of the military's policing them, of the government's bringing troops against them instead of against national enemies, such as the French and the Spanish. This horror dates back centuries, to the Norman invasion of England in 1066, when an army under William the Conqueror devastated the countryside. The soldiers robbed, raped, burned, and brutalized, committing all the atrocities at which armies excel. Then, their victory secure, they added insult to injury by quartering their troops on the native Saxons. They also taxed them.

The Saxons contrasted this abuse by professional soldiers with the behavior of their own militias. Saxon farmers and shopkeepers fought to defend themselves when attacked, but they returned to their farms and shops once the danger had passed. They did not make a career of robbing people on behalf of the king, nor did they burn a man's home and sack his shop. Militias were defensive, armies offensive: the difference keenly impressed Saxon farmers pondering plundered towns, farms in flames, and wives and daughters traumatized or even dying from rape.

This martial skepticism was reinforced during the civil wars of the 1600s, especially Oliver Cromwell's military dictatorship. A "standing army," with its professional killers and its existence even during peacetime, was considered the worst evil that could afflict a free people—if a people so afflicted could be called free.

By the eighteenth century this national attitude resulted in a poorly manned army of thin ranks. Add to this an abusive command relying on physical torture and low pay to control the soldiers, and it's no wonder the British army had to resort to kidnapping to fill its brigades. It drafted almost literally out of the gutter those soldiers it didn't take from the hangman. (Judges sometimes offered convicted murderers and other miscreants a choice between killing for the King or being killed.)

Recruits who weren't ducking the scaffold usually came from society's lowest rungs. Impressment officers prowled the streets of London, promising the naked, starving underclass a warm uniform and regular rations. When these blandishments failed, the officer tried to get his victim so drunk he would grasp a shilling: astoundingly, the government considered that pittance a fair exchange for a man's life. You might think it easy to slip a coin into a poor man's hand, especially one plied with free booze all night. But however brutal life on the streets was, everyone knew the army was worse. Nor was there any escape: once a soldier, always a soldier. It took death to free a man from his "deal" with the King.

Citizens feared the army drawn from such ranks much as we would a mob from our slums and penitentiaries. Perhaps a beggar or prisoner with the soul of a poet was recruited now and then, but if so, he was rapidly desensitized once he donned his uniform. Discipline was draconian, merciless, excessive, terrifying—we can exhaust the thesaurus and still not come close to describing the torture regularly inflicted on the poor cuss turned soldier or sailor. The most minor of transgressions earned horrific retribution, with flogging the favored punishment. These whippings consisted of hundreds of lashes and sometimes a thousand; they were so savage they could kill or, at the least, cripple the victim for life. Often the lashes were administered in sets over the course of several weeks or a month: this allowed the muscles (little skin would be left after the first strokes from the cat-o'-nine-tails) of the back to begin healing before they were once again ripped open. When the brutality finally ended and the victim's wrists were loosed from the crossed halberds, a bucket of salt water was dashed across him—a crude and unspeakably cruel antiseptic.

Men abused so horrifically were unlikely to show mercy, kindness, or empathy to the civilians who crossed their paths. Governor Hutchinson described those in one of the two regiments loosed on Boston: "They are

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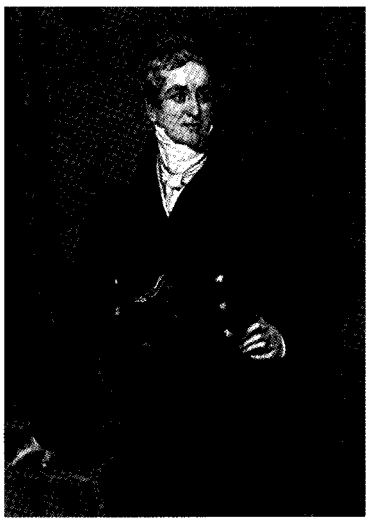
in general such bad fellows in that regement [sic] that it seems impossible to restrain them."[11] An unbridgeable gap yawned between "citizen" and "soldier," and though these men might protect England from France's vengeance, most Englishmen felt little gratitude for this "service." Britain engaged in many of the trade restrictions that our government does, spawning a century's worth of war. This benefited the same politicians, bureaucrats, and manufacturers of armaments that current wars do. Everyone else realized the army guarded the interests of these groups at his expense—literally. Nor did people swallow any line about the troops' "protecting" their liberty: these same soldiers also quelled civilians who rioted in protest of the government's policies.

In some ways, using soldiers may have been friendlier to freedom than a dedicated police force. Sending troops against a citizenry that feared the army kept folks continually on their guard against them. Anyone who tried to portray these armed aliens as allies, in league with honest citizens to defend society from the bad guys, would have been dismissed as a fool.



Robert Peel

Robert Peel

Then along came Robert Peel, MP, creator of England's first police force.

Born in 1788, Peel joined Parliament as a Tory in 1809. His career there hopscotched between the party line and independence. This allows admirers to portray him as principled, while those who understand political power consider him adept at manipulating it. In 1812, as chief secretary for Ireland, he instituted the "Peace Preservation Police." Ireland foamed then as now with religious-cum-political conflicts, so "peace preservation" translated to quashing resistance to the decrees of King and Parliament.

Peel's police quashed so successfully that he was appointed home secretary in 1822. This was a troubled decade in England; four years later, a depression crippled the country. Predictably, crime and rioting increased with unemployment, especially in the cities. But, again predictably, this did not sway government to end the mercantilism causing the depression. Instead, as would any astute politician already famous for "solving" a similar problem, Peel called for a committee to investigate the possibilities of a police force in London.

Unfortunately for Peel, the committee wasn't as astute as he. The first time around it reported that police were by their nature inimical to a free society. Peel sent them back to the drawing board for a more acceptable answer. Not surprisingly, the committee then recommended that the government should act. Specifically, it should organize and augment London's existing officers.

There were about 450 of these, ranging from magistrates' "runners" to Marine Police patrolling the Thames for contraband and untaxed goods. Peel consolidated these agents, hired enough new men to bring his number to 1,000, trained them, and put them in uniform as well as on the public's purse.

Peel also codified nine principles for his police. These ranged from a mission statement (the purpose of the "peelers" or "bobbies," as they were called in Peel's honor, was to prevent crime and keep the peace) to the practical tip of securing the public's cooperation through impartiality and courtesy. But one of Peel's Principles struck liberty a blistering blow. For the first time, instead of the state's agents being hurtful and alien, a force snatched from prison and poverty and turned loose on the public by a vengeful king, the bobbies were instead to pose as friends and neighbors. "The police," Peel insisted, "are the public and the public are the police; the police being only members of the public who are paid to give full-time attention to duties which are incumbent on every citizen in the interest of community welfare and existence."[12]

The new bureaucracy, complete with two commissioners, was up and running by 1829. Given London's crime wave, it seems reasonable to assume that law-abiding folk welcomed these guardians. Instead, they despised them. Nor did they cooperate with them. They called the bobbies by names far more Anglo-Saxon, sometimes assaulted them, and occasionally killed them.

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A jury even returned a verdict of "justifiable homicide" for a civilian charged with murdering one.

But just as a man gets used to hanging, so Londoners did to bobbies. Their hostility faded with time. Actually, the public's feelings about these "members . . . paid to give full-time attention to duties which are incumbent on every citizen" probably little mattered when it came to continuing the bobbies' patrols: an ostensibly free country now had an unanswerable excuse—protecting citizens from nongovernmental criminals—for infiltrating and monitoring the population. It would hardly relinquish this immense advantage without prolonged, mass rebellion.

Other governments eagerly watched Britain's experiment with the intent of copying it. The first American city to do so was New York, in 1853. We might hope that a country founded in freedom would resist paying some citizens to enforce the state's whims against others. Instead, Philadelphia boasted a force by 1856 and Boston by 1859, despite its rioting just 90 years before against red-coated police. Perhaps the blue coats lulled suspicion.

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Preventing Crime

Americans heard the same excuses for the state's monitoring them as Londoners had—the same excuses, in fact, which prevail today: the police would keep the peace and prevent crime. Never mind that the police have a questionable record of solving, let alone preventing, crime. Typically, police departments in large cities "solve" only 55–65 percent of homicides, though that doesn't necessarily include apprehending the culprit. Governments have long resorted to asking, even haranguing, the public for help in solving crime; many now host websites listing their failures in the hopes that citizens will ride to the rescue.[13] And despite New York City's phalanx of 40,000 cops—an army larger than George Washington ever commanded at one time during the Revolutionary War—17,875 cars were stolen in 2005, a "sharp drop" from previous years.[14]

Broken promises have never threatened the existence of police departments, however. That's because these institutions are extremely useful to the politicians who determine their fate. With the advent of New York City's first force, politicians rejoiced at having an entire department of voters depend on them for a raise; even more did they appreciate the management positions they could award to influential supporters. They often looked on their city's cops as political bodyguards, akin to Caesar Augustus's praetorian guard: during elections, cops made sure the "right" folks voted.

Civil-service rules supposedly eliminated such corruption in the late nineteenth century, but any improvements were offset by the police's expansion into everyday life. Their consistent presence on the streets attracted the attention of anyone wanting help. Folks who might have relied on family and neighbors turned instead to the patrolman in his noticeable uniform. Police were soon chaperoning lost children, adjudicating domestic disputes, controlling traffic, and even boarding bums in their station houses. Official involvement elevated these matters, sometimes serious but often merely mundane, into crises worthy of their own bureaucracies, fertilizing the growth of municipal governments.[15]

In contrast to their eighteenth- and early-nineteenth-century forefathers, modern Americans take police for granted, much like driver's licenses and parking tickets. If they think about them at all, it is not as a standing army quartered among them but as heroes who serve and protect. Even the latest corruption scandal or physical abuse of a prisoner scarcely dents the apathy and mistaken perception. Those who do rail against corruption and abuse seldom question the basic premise behind policing; instead, all that's required is weeding out the rogues, tinkering with the regulations, and reforming the department yet again.

This is especially tragic given the warped emphasis policing brings to crime. The American judicial apparatus focuses on punishing those who transgress the government's decrees, either extracting their money for the state or imprisoning them or both. Restoring the criminal's victim is hardly ever a consideration (perhaps because most "crimes" the state now prosecutes actually

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have no victims). This contrasts baldly and badly with Anglo-Saxon justice, in which making the victim whole was the sole concern.[16] Neighbors mutually pledged to assist anyone who suffered loss at the hands of a thief or murderer. Once the miscreant was apprehended, the community assessed his guilt and, if satisfied, required him to make restitution. Those criminals who refused faced ostracism, leaving them vulnerable to vengeance from their victims.

Occasionally, a violator was stronger than the community on which he preyed, at which point folks might solicit the king's help. Early Anglo-Saxon kings maintained a palace guard, though these forces were small in number because the king paid them from his own pocket. Communities began including a royal recompense, then, in the violator's restitution. But the royal eye quickly recognized a river of revenue in that recompense. This created a perverse incentive to invent more "crimes" with large fines. Gradually, the state arrogated to itself a monopoly on "solving" crime, with its profits trumping the victim's restitution. That left folks with little reason to report misdeeds beyond the hope that the criminal, if caught, would no longer prey on them, and they quit doing so. The state had the last laugh, though: it became a crime not to report a crime. This permeates practically all American penal codes to this day.

Obviously, government's interest lies in persuading taxpayers that the police protect them not the state. But the priorities are obvious. How many dollars of stolen goods are returned to citizens versus how many dollars in traffic tickets go to the state?[17] How many political demonstrations are "contained" by the police versus how many stolen cars are recovered? How often is a senator or governor coddled by a police escort when he descends on a town versus how many ordinary folks fear to venture down a dark alley? Indeed, New York City's percentage of "solved" murders in 2005 plunged perhaps because so many detectives were busy protecting visiting pooh-bahs. Clearly, the state profits far more from the police than do the people.

I once watched a trial in which a policeman was suing the police force that had employed him. He had been fired a few days before he would have retired. This brought his pension in doubt, which in turn brought him into court. His attorney emphasized his client's valor by insisting that for 20 years he had performed "paramilitary" duties with a "paramilitary" force. He consistently and repeatedly portrayed the police as "paramilitary."

Tragically, that makes us the "para-enemy."

1. Mercy Otis Warren, *History of the Rise, Progress and Termination of the American Revolution*, vol. I. (Indianapolis: Liberty Fund, 1994), p. 38.

2. Esther Forbes, *Paul Revere and the World He Lived In* (Boston: Houghton Mifflin Company, 1942), p. 137.

3. Otis Warren, pp. 54–55.

4. Page Smith, *A New Age Now Begins: A People's History of the American Revolution* (New York: McGraw-Hill, 1976), p. 303.

5. Ibid., p 319.

6. Ibid., p. 305.

7. Ibid., p. 334.

8. Ibid., pp. 338–39.

9. Forbes, p. 172.

10. Smith, p. 340.

11. Forbes, p. 142.

12. See http://72.14.203.104/search?q=cache:A4Cw6PjFGlcJ:www.bulkley.net/

13. For an example, see Manchester, N.H.'s list of outstanding murders at www.manchesternh.gov/CityGov/MPD/CrimeData/Unsolved.html.

14. "A Stolen Love Is Found, 37 Years Down the Road." *New York Times*, January 17, 2006.

15. See "Police Forces" in Eric Foner and John Garraty, eds., *The Reader's Companion to American History* (Boston: Houghton Mifflin, 1991).

16. Ireland, Iceland, and "the large number of primitive societies anthropologists have studied" value restitution instead of punishment too, according to Bruce Benson. He also points out that in addition to making the victim whole, restitution offers two other benefits: it does not force taxpayers to subsidize criminals' room and board, clothing, and guards, and it eliminates "crimes" of vice since these involve only willing participants, not victims. Download Benson's article "Crime" here: http://garnet.acns.fsu.edu/%7Ebbenson/crime.doc.

17. Because municipalities often try to hide their income from traffic tickets so they don't have to divide the plunder with their respective states, no one knows how much money tickets generate each year. The National Motorists Association (NMA) estimates that state and local governments are raking in between $3.75 and $7.5 *billion* annually–and that excludes parking tickets. Hand-in-glove with governments on this issue are insurance companies, which raise their rates for "unsafe" motorists. These penalties are so lucrative that insurance companies often donate radar detectors and other such equipment to police departments. The NMA's website offers illuminating facts and statistics on traffic laws as well as tips on fighting tickets: www.motorists.org/index.html.

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The Jewel of Consistency

BY FRED DE ARMOND

The strangest thing about this century's collectivist revolution is the amazing discrepancy between words and actions. In the abstract, men speak with the tongues of angels; in the concrete, their actions are often Mephistophelian. If even 51 percent of those who express stout devotion to liberty and opposition to State socialism had acted and voted as they talked, the revolution would have died a-borning.

Nearly everyone professes loyal devotion to the Constitution—until he starts to translate that devotion into action. "The maximum of local self-government" is an unchallenged adage—until an appropriation is demanded from Washington.

Examples parade in endless procession.

Labor leaders breathe fire and fury on the dangers of business monopoly. Big Business, they say, is erecting a great oligarchy that is crushing free competition and hamstringing our liberties. But in the very next breath they argue passionately that independent unions should be suppressed by law, not permitted to compete with the AFL-CIO. Nor, they add with equal heat, does a dissenting worker have the right to decline union membership.

Not to be outdone in inconsistency, a formidable body of businessmen who oppose government fixing of wages are equally vocal in demanding government fixing of prices. Businessmen have with good reason opposed rigid "parity" price subsidies to farmers, as a form of encroaching socialism. But is "cheap" federal electric power, for which so many businessmen clamor, any less a subsidy than parity payments to farmers? In both cases, the difference between free-market prices and artificial, government-manipulated prices is drawn from the well of public funds that come from taxation. Direct government competition with the electric power industry is a clear invitation to the collectivists to socialize other industries as well as power.

Who has joined in logrolling for federal grants with more zeal than businessmen? Whether to states or communities, whether for airports, highways, street improvements, high dams, new post offices, or aid to education, federal grants are an essential part of the Keynesian policy of Fabian socialism. And yet, how many Chamber of Commerce delegations stifle their principles in order to journey to Washington and stand in line for these handouts!

Businessmen are probably no more inconsistent ideologically than farmers, professionals, and workers. But by all logic and strategy, they should be out front raising a standard of consistency. Because of their position in society, particularly in America, their failure to hew to the line sets a conspicuous and what might well be a fatal example. Since business has so much at stake in a free competitive society, it should step forward in demonstrating the fullest devotion to the principle of individualistic competition. State paternalism is affirmed in all business circles to be a deadly threat to free enterprise and republican government. But businessmen, individually and in groups, continue to ask for government intervention in the economic sphere.

The opposition to collectivism has fumbled again and again because it has been consistently inconsistent. The doctor who won't take his own medicine or the

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lawyer who disregards his own counsel is bound to be less than convincing.

On the other hand, in one notable respect every move made by the collectivists has fitted into a consistent pattern. That is their leveling urge. The key and nucleus of the whole movement toward statism is to take away from some and give to others. No one has phrased this mania quite so lucidly as William Graham Sumner: "A and B put their heads together to decide what C shall do for D." Analyze down to its sources every "liberal" measure and somewhere in it you will find this basic motivation. It rests on the prime fallacy of the ages, as stated in all its ugly simplicity by the French Revolutionist Babeuf: "We know that every man has an equal right to the enjoyment of every benefit."

If the true liberals of our time—robbed even of their traditional label by the devious semantic arts of the socialists—are to win acceptance in the minds of men, they will have to agree on a few affirmative principles as simple and as fundamental as Babeuf's. But, what is much more than that, they will have to go down the line and live by those principles.

When a businessman, farmer, labor leader, or professional man asks for a "break" from government in his struggle with competition, he is so far inconsistent—if he professes faith in free enterprise. He has opened himself to an unanswerable counterattack by those who contend that the competitive system is ruthless and exploitative, not to be trusted. And it is no defense to say, "Everyone else is getting help; the only way I can keep up is to get mine." This amounts to a defeatist concession that socialism is inevitable.

The acid test for businessmen comes in those no-quarter contests between such competitive groups as railroads and truckers, coal and gas, stock companies and mutuals, chain stores and independents, and the never-ending truculence of "small business" toward "big business." Can not these competitive tests of ability be carried on without asking for the intervention of government?

> Who has joined in logrolling for federal grants with more zeal than businessmen? Whether to states or communities, whether for airports, highways, street improvements, high dams, new post offices, or aid to education, federal grants are an essential part of the Keynesian policy of Fabian socialism.

Consistency No Virtue?

Today, of course, we have to contend with those who claim that consistency is not a virtue. They are fond of citing Emerson's oft-quoted epigram in support of that position. The great Transcendentalist fathered a brood of errors in that passing remark. But it is fair to recall that Emerson did not say, "Consistency is the hobgoblin of little minds." He qualified his paradox by making it "a foolish consistency." It is also worth noting that in his *Journal* entry for September 29, 1838, the Concord philosopher deplored inconsistency.

The truth about consistency was better stated more than two millenniums earlier by Confucius, who said, "A gentleman is consistent, not changeless."

By the traditional and time-honored ethic, methods and policies can often be compromised successfully; principles cannot. That is where the issue is joined. Today's pragmatists do not accept that view. They hold that there are no principles so vital that they must be adhered to under all circumstances, hence that there is no virtue in consistency. Anything that "works" is justifiable. The innovators are to be the judges of what works.

As Confucius suggested, men may properly change their methods and policies. They may even change their principles. But when one fails to act in conformance with the principles he professes, he is guilty of something akin to a moral lapse.

In stating his theory of compromise, John Morley wrote that "he who begins life by stifling his convictions is in a fair way for ending it without any convictions to stifle."

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But the inconsistency that is such an Achilles' heel of American conservatives springs more from foggy thinking and shortsighted expediency than from a true moral lapse. To be consistent, one has to start with certain principles that he will not surrender, even for temporary advantages that might result from compromise. Then one must follow the implications of these principles when put in practice. This second step is the catch of the formula because it calls for the exercise of both intelligence and character.

In a very suggestive sentence of his splendid guide to *The Art of Thought* Graham Wallas has indicated a simple method for plotting a consistent course in a situation that requires a choice. If you suspect that two propositions which you have heretofore accepted as true seem to conflict with each other, examine the natural implications of both until the point of divergence is located. Then follow the one that leads in the same direction as your irreducible principles, and resolutely abandon the other proposition.

What leads men into ideological inconsistencies?

The first cause is a blind devotion to immediate pecuniary interests. In business, the bird in hand is not always worth two in the bush. A businessman, for instance, may have to sacrifice here and there for his principles. Usually, the sacrifice will be one of temporary gain for long-run good.

Personal and Group Loyalties

The second cause is confusion as to personal and group loyalties. A man may act against his better judgment, submerge his views, because he is reluctant to differ from friends or family or cherished leaders. Or it may be that he is constrained to hold his nose and go along rather than break with his political party or his church. This kind of action cannot be justified if one is asked to swallow a fallacy or support a fraud that he can't square with the irreducible principles by which his faith and practice are guided. Then he must shake off old loyalties, even if he stands alone.

It must be granted that all organized political action involves compromise. Very often it will appear to any conscientious citizen that he must vote for men and measures which are but the lesser of two evils. But if this is the price that must be paid for political reconciliation of diverse views, then it behooves each of us to look that much harder for nonpolitical alternatives that do not require our voting for an evil.

But if compromise is the price that must be paid for political reconciliation of diverse views, then it behooves each of us to look that much harder for nonpolitical alternatives that do not require our voting for an evil.

The inconsistency in political action comes in what John Morley called "a lazy accommodation with error, an ignoble economy of truth," in which we settle for less than the best of which we are capable, because we lack the toughness of mind and character to exert ourselves for truth and right as we see them.

It has become a popular fetish to boast that "I vote for the man, not the party." And, of course, it is important that political power be vested in men of high character and integrity. But this alone will not avert bad government—not if the political technique of deciding by ballot between two evils is thoughtlessly applied when a positively good alternative might have been available. To vote for the man who will most fairly "redistribute the wealth" is and will always be wholly inconsistent with such principles as private ownership and control of property and voluntary exchange between willing buyers and sellers.

Consistency is the jewel that would bring together men of like minds on the issues that really count. Back in Civil War days in the North there was a slogan, "Vote like you shoot!" That crude admonition might be paraphrased to fit today's crisis: Vote and act like you talk!

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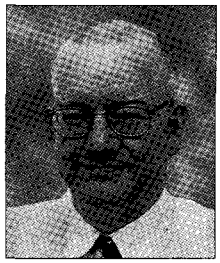
The History of "Underdevelopment"



BY STEPHEN DAVIES

Perhaps the most important feature of the modern world is its sustained, intensive economic growth. This produces most of the other distinctive features of modernity. Although there were earlier episodes of such economic efflorescence (to use Jack Goldstone's term), it was only with the "industrial revolution" of late eighteenth-century Britain that it became a permanent and prominent feature of the world economy. Following the advent of this transformative process, questions soon arose elsewhere. The first was that of how to achieve the same kind of growth and dynamism. Soon this led to further questions: why other parts of the world did not show these qualities and why their attempts to do so ended in failure.

The debate engendered by these questions and the answers given has been one of the most important of the last 200 years. Known as the "development debate," it consists of such topics as the nature and causes of economic development and the reasons it occurs at some times and places but not others. This is not simply an academic debate. It has obvious implications for public policy and, through its impact on policy, for the lives and circumstances of ordinary people.

Since the early 1950s much of this debate has been dominated by "dependency theory" and its offshoot "world system theory." Developed by several people, this was a theory that explained the economic success or failure of different parts of the world by the nature and structure of the economic relations among them. The argument is that the relations of trade between different parts of the world are inherently exploitative and inevitably create inequality and lack of development in certain places. Certain parts of the world (the "core") dominate high technology and high profit activity such as manufacturing. The rest (the "periphery") is left to produce raw materials and primary products.

This means that while some parts are "developed" and experience economic modernization, other parts are unable to do so and thus remain "undeveloped." They may even experience "underdevelopment" in which their level of prosperity and economic organization actually goes into decline. The advantage of this theory is that it leads to a focus on the world as a whole, rather than concentrating on "national" economies that have no real existence. Its disadvantages are that it misunderstands much of what it tries to explain and, even more serious, that it generates policy proposals that are disastrous. It leads to a series of policy proposals—including import substitution, a ban on foreign investment, and protectionism combined with extensive state ownership—that have failed wherever they have been tried.

> This dynamic and benign process was stopped by World War I and did not subsequently resume. The war seriously disrupted the international monetary and trade system. Even worse were the political effects.

Why though did this analysis prove so popular? It identified and offered an explanation for something that conventional theory either ignored or had problems explaining: the way in which the diffusion of economic modernization, which had been going on steadily up to the early twentieth century, suddenly stopped and even went into reverse. Following the appearance of economic modernity in Britain, other parts of the world also underwent a similar transformation. By 1910 these included Belgium, the Netherlands,

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northern Italy, Germany, the United States, Japan, France, Sweden, Denmark, Russia, Argentina, and Uruguay. Not all these cases involved industrialization and a shift toward manufacturing: this had not been the case in France, nor in places such as Denmark or Argentina, which had become highly efficient producers of agricultural products.

However, after 1914 the process came to a stop. As Peter Drucker pointed out, between 1910 and 1970 no new country joined the list of "developed" nations and some (notably Argentina) fell off it. Instead a large part of the world appeared unable to start the process of sustained growth. Dependency theory offered both an explanation for this and a prescription for resolving the problem. In fact, there was a much simpler explanation, which history provided. This was that the check to the spread of modernization was caused by a combination of two factors. The first was mistaken economic policy by governments, particularly those actually intended to promote growth. The other was macro-level disruption of the world economy during the central decades of the twentieth century, which slowed down the processes that had led to the spread of modernization in the nineteenth century and affected even those countries that had not adopted wrongheaded policy themselves.

During the nineteenth century not every attempt at modernization succeeded. Besides the "hits" mentioned earlier, there were a number of "misses." These typically involved attempts at precisely the program of state-led and autarkic industrialization advocated by the dependency theorists. Examples of this included Paraguay (under Dr. Francia) and Egypt (under Mehmet Ali). The growth of the world economy as a whole at this time and the spread of economic modernity were driven by interlinked processes, all of which operated on a global scale. These were a rise in the volume of trade, both absolutely and as a relative proportion of total activity; a growth in investment outside the area of capital formation; a sharp increase in the geographical mobility of labor; increased economic integration and specialization; and rapid technological innovation and diffusion of new technology—interestingly, the last was marked by a weakening of the status of intellectual property rather than the reverse.

These processes both stimulated and were in turn driven by the economic and social transformation of ever larger areas of the planet. So dynamic had the world economy become by the 1900s that some fortunate parts of the world were "developed" despite mistaken policies by their ruling elites.

Stopped by War

However, this dynamic and benign process was stopped by World War I and did not subsequently resume. The war seriously disrupted the international monetary and trade system. Even worse were the political effects. Everywhere there was a move in the direction of state control and economic nationalism. This reflected both the influence of mistaken ideas and the interests of elites whose position was threatened by economic change. A series of policy errors brought about an unprecedentedly severe slump and then prolonged it, with disastrous effects on worldwide growth and trade. This was felt most severely in parts of the world that had just started the process of modernization before 1914. The two classic cases were China and India. Recent research shows that both China and India were experiencing rapid economic development between 1870 and 1914. Had this continued, both would have joined Japan in the "developed" club by the 1930s at the latest. However their development was cut short by the disasters of 1914 to 1945.

The paradox is that the prescriptions for resolving "underdevelopment" actually made the problem worse. India is the classic example, with the policy of successive administrations from Nehru onward proving completely unsuccessful in reigniting the rapid growth India had enjoyed during the "Belle Epoque." However, today the arguments of the dependency school are discredited. The reason is simple: since the late 1980s the process described above has resumed and several governments, above all those of China and India, are no longer obstructing it. Consequently the last 16 years have seen the largest decline in absolute poverty ever. For economic historians the years between 1914 and 1990 increasingly look like a tragic detour or diversion from the path of development. However, some still see the process as undesirable, and many elite groups still frantically try to control it in their own interests.

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Ludwig von Mises: The Political Economist of Liberty

PART II

BY RICHARD M. EBELING

In *Socialism* (1922), *Liberalism* (1927), and *Critique of Interventionism* (1929), the task Ludwig von Mises set for himself was to offer a radically different vision of man in society from that presented by the socialists, nationalists, and interventionists. In place of their starting premise of inescapable conflicts among men in terms of "social class," nationality and race, or narrow group interest, Mises insisted that reason and experience demonstrated that all men could associate in peace for their mutual material and cultural betterment. The key to this was an understanding and appreciation of the benefits of a division of labor. Through specialization and trade the human race has the capacity to lift itself up from both poverty and war.

Ludwig von Mises

Men become associates in a common process of social cooperation, instead of antagonists with each attempting to rule over and plunder the others. Indeed, all that we mean by modern civilization, and the material and cultural comforts and opportunities that it offers man, is due to the highly productive benefits and advantages made possible by a division of labor. Men collaborated in the arena of competitive market exchange.

The confusion, Mises pointed out, is the failure to view this cooperative social process from a longer-run perspective than the changing circumstances of everyday life. In the rivalries of the market, there are always some who earn profits and others who suffer losses in the interactive and competitive processes of supply and demand. But what needs to be understood is that these changes in the short-run fortunes of various participants in the division of labor are the method through which each participant is informed and nudged into either doing more of some things or less of others. This process brings about the necessary adjustment of society's productive activities in order to assure that they tend to match and reflect the market pattern of consumer demand.[1]

Of course, political force can be substituted for the "reward" of profits and the "punishment" of losses. However, the costs of this substitution are extremely high, Mises argued. First, men are less motivated to apply themselves with intelligence and industry when forced to work under the lash of servitude and compulsion, and thus society loses what their free efforts and invention might have produced.[2] Second, men are forced to conform to the values and goals of those in command, and thus they lose the liberty of pursuing their own purposes, with no certainty that those who rule them know better what may give them happiness and meaning in life.

And, third, socialist central planning and political intervention in the market, respectively, abolish or distort the functioning of social cooperation. A sustained and extended system of specialization for mutual improvement is only possible under a unique set of social and economic institutions. Without private ownership in the means of production, the coordination of multitudes of individual activities in the division of labor

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is impossible. Indeed, Mises's analysis of the "impossibility" of a socialist order being able to match the efficiency and productivity of a free-market economy was the basis for his international stature and reputation as one of the most original economists of his time, and was the centerpiece of his book *Socialism*.[3]

Private ownership and competitive market exchange enable the formation of prices for both consumer goods and the factors of production, expressed in the common denominator of a medium of exchange—money. On the basis of these money prices, entrepreneurs can engage in economic calculation to determine the relative costs and profitability of alternative lines of production. Without these market-generated prices, there would be no rational way to allocate resources among their competing uses to assure that those goods most highly valued by the buying public were produced in the least costly and therefore most economical manner. Economic calculation, Mises demonstrated, guarantees that the scarce means available best serve the members of society.

Private ownership and competitive market exchange enable the formation of prices for both consumer goods and the factors of production, expressed in the common denominator of a medium of exchange—money.

Such rationality in the use of means to satisfy ends is impossible in a comprehensive system of socialist central planning. How, Mises asked, will the socialist planners know the best uses for which the factors of production under their central control should be applied without such market-generated prices? Without private ownership of the means of production there would be nothing (legally) to buy and sell. Without the ability to buy and sell, there will be no bids and offers, and therefore no haggling over terms of trade among competing buyers and sellers. Without the haggling of market competition there would, of course, be no agreed-on terms of exchange. Without agreed-on terms of exchange, there are no market prices. And without market prices, how will the central planners know the opportunity costs and therefore the most highly valued uses for which those resources could or should be applied? With the abolition of private property, and therefore market exchange and prices, the central planners would lack the necessary institutional and informational tools to determine what to produce and how, in order to minimize waste and inefficiency.

Mises Challenged

Socialists and many nonsocialist economists claimed over the decades that Mises was wrong when he said that socialism was "impossible." They pointed to the Soviet Union and said it existed and operated. However, in numerous places in his various writings, beginning from the early 1920s, Mises insisted that he was not saying that a socialist system could not exist. Of course, the factors of production could be nationalized and a central planning agency could be delegated the responsibility to direct all the production activities of the society.

But any supposed rationality and seeming degree of efficiency observed in the workings of the Soviet and similar socialist economies was due to the fact that such socialist planning systems existed in a world in which there were still functioning market societies. The existing market economies provided various "shadow prices" that the socialist planners could try to use as proxies and benchmarks for evaluating their own allocation and production decisions. However, since the actual economic circumstances in such a socialist economy would never be an exact duplicate of the conditions in the neighboring market societies—resource availabilities, labor skills, the quantity and qualities of capital equipment, the fertility and variety of land, the patterns of consumer demand—such proxy prices could never completely "solve" the economic calculation problem for the socialist planners in places like the Soviet Union.[4]

Therefore, Mises declared in 1931, "From the standpoint of both politics and history, this proof [of the 'impossibility' of socialist planning] is certainly the most important discovery by economic theory. . . . It alone

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will enable future historians to understand how it came about that the victory of the socialist movement did not lead to the creation of the socialist order of society."[5]

At the same time, Mises demonstrated the inherent inconsistencies in any system of piecemeal political intervention in the market economy. Price controls and production restrictions on entrepreneurial decision-making bring about distortions and imbalances in the relationships of supply and demand, as well as constraints on the most efficient use of resources in the service of consumers. The political intervener is left with the choice of either introducing new controls and regulations in an attempt to compensate for the distortions and imbalances the prior interventions have caused, or repealing the interventionist controls and regulations already in place and allowing the market once again to be free and competitive. The path of one set of piecemeal interventions followed by another entails a logic of the growth of government that eventually would result in the entire economy coming under state management. Hence, interventionism consistently applied could lead to socialism on an incremental basis.[6]

The most pernicious form of government intervention, in Mises's view, was political control and manipulation of the monetary system. Contrary to both the Marxists and the Keynesians, Mises did not consider the fluctuations experienced over the business cycle to be an inherent and inescapable part of the free-market economy. Waves of inflations and depressions were the product of political intervention in money and banking. And this included the Great Depression of the 1930s, Mises argued.

Monetary Manipulation

Under various political and ideological pressures, governments had monopolized control over the monetary system. They used the ability to create money out of thin air through the printing press or on the ledger books of the banks to finance government deficits and to artificially lower interest rates to stimulate unsustainable investment booms. Such monetary expansions always tended to distort market prices resulting in misdirection of resources, including labor, and malinvestment of capital. The inflationary upswing caused by an artificial expansion of money and bank credit sets the stage for an eventual economic downturn. By distorting the rate of interest, the market price for borrowing and lending, the monetary authority throws savings and investment out of balance, with the need for an inevitable correction. The "depression" or "recession" phase of the business cycle occurs when the monetary authority either slows downs or stops any further increases in the money supply. The imbalances and distortions become visible, with some investment projects having to be written down or written off as losses, with reallocations of labor and other resources to alternative, more profitable employments, and sometimes significant adjustments and declines in wages and prices to bring supply and demand back into proper order.[7]

> There is no alternative to a thoroughgoing unhampered free-market economy, including a market-based monetary system such as the gold standard.

The Keynesian revolution of the 1930s, and which then dominated economic policy discussions for decades following World War II, was based on a fundamental misconception of how the market economy worked, in Mises's view. What Keynes called "aggregate demand failures" to explain the reason for high and prolonged unemployment distracted attention away from the real source of less-than-full employment: the failure of producers and workers on the "supply side" of the market to price their products and labor services at levels that potential demanders would be willing to pay. Unemployment and idle resources constitute a pricing problem, not a demand-management problem. Mises considered Keynesian economics basically to be nothing more than a rationale for special-interest groups, such as trade unions, that didn't want to adapt to the reality of supply and demand and of what the market viewed as their real worth.[8]

Thus Mises's conclusion from his analysis of socialism and interventionism, including monetary manipulation, was that there is no alternative to a thoroughgoing

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unhampered free-market economy, including a market-based monetary system such as the gold standard.[9] Both socialism and interventionism are, respectively, unworkable and unstable substitutes for capitalism. The classical liberal defends private property and the free-market economy, he insisted, precisely because it is the only system of social cooperation that provides wide latitude for freedom and personal choice to all members of society, while generating the institutional means for coordinating the actions of billions of people in the most economically rational manner.

Classical Liberalism, Freedom, and Democracy

Mises's defense of classical liberalism against these various forms of collectivism, however, was not limited "merely" to the economic benefits from private property. Property also provides man with that most valuable and cherished object—*freedom*. Property gives the individual an arena of autonomy in which he may cultivate and live out his own conception of the good and meaningful life. It also protects him from dependency on the state for his existence; through his own efforts and voluntary exchange with other free men, he is not beholden to any absolute political authority that would dictate the conditions of his life. Freedom and property, if they are to be secure, require *peace*. Violence and fraud must be outlawed if each man is to take full advantage of what his interests and talents suggest would be the most profitable avenues to achieve his goals in consensual association with others.

Mises's defense of classical liberalism against these various forms of collectivism was not limited "merely" to the economic benefits from private property.

The classical-liberal ideal also emphasizes the importance of *equality before the law*, Mises explained. Only when political privilege and favoritism are eliminated can each man have the latitude to use his own knowledge and talents in ways that benefit himself and also rebound, through the voluntary transactions of the market, to the betterment of society as a whole. This means, at the same time, that a liberal society is one that accepts that *inequality of income and wealth* is inseparable from individual freedom. Given the diversity of men's natural and acquired abilities and volitional inclinations, the rewards earned by people in the marketplace will inevitably be uneven. Nor can it be otherwise if we are not to diminish or even suffocate the incentives that move men to apply themselves in creative and productive ways.

The role of government, therefore, in the classical-liberal society is to respect and protect each individual's right to his life, liberty, and property. The significance of *democracy*, in Mises's view, is not that majorities are always right or should be unrestrained in what they may do to minorities through the use of political power. Elected and representative government is a means of changing who holds political office without resort to revolution or civil war. It is an institutional device for maintaining social peace. It was clear to Mises from the experience of communism and fascism, as well as from the many tyrannies of the past, that without democracy the questions of who shall rule, for how long, and for what purpose would be reduced to brute force and dictatorial power. Reason and persuasion should be the methods that men use in their dealings with one another—both in the marketplace and the social and political arenas—and not the bullet and the bayonet.[10]

In his book on classical liberalism Mises bemoaned the fact that people are all too willing to resort to state power to impose their views of personal conduct and morality whenever their fellow human beings veer from their own conception of the "good," the "virtuous" and the "right." He despaired, "The propensity of our contemporaries to demand authoritarian prohibition as soon as something does not please them . . . shows how deeply ingrained the spirit of servility still remains in them. . . . A free man must be able to endure it when his fellow men act and live otherwise than he considers proper. He must free himself from the habit, just as soon as something does not please him, of calling for the police."[11]

What, then, should guide social policy in determining the limits of government action? Mises was a utili-

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tarian who argued that laws and institutions should be judged by the standard of whether and to what extent they further the goal of peaceful social cooperation. Society is the most important means through which men are able to pursue the ends that give meaning to their lives. But Mises was not what has become known in philosophical discussion as an *act-utilitarian*; that is, one who believes that a course of action or a policy is to be determined on an ad hoc, case-by-case basis. Rather, he was a *rule-utilitarian*, one who believes that any particular course of action or policy must be evaluated in terms of its consistency with general rules of personal and social conduct that reason and experience have accumulated as guides to conduct. Any action's long-run consequences must be taken into consideration in terms of its consistency with and relationship to the preservation of the institutions essential for successful social interaction.[12] This is the meaning of the phrase Mises often used: the "rightly understood long-run interests" of the members of society.[13]

Thus his defense of democracy and constitutional limits on the powers of government was based on the reasoned judgment that history has demonstrated far too many times that the resort to nondemocratic and "extra-constitutional" means has led to violence, repression, abrogation of civil and economic liberties, and a breakdown of respect for law and the legal order, which destroys the long-run stability of society. The apparent gains and benefits from "strong men" and "emergency measures" in times of seeming crisis have always tended to generate costs and losses of liberty and prosperity in the longer run that more than exceed the supposed "short-run" stability, order, and security promised by such methods.

Classical Liberalism and International Peace

The benefits from social cooperation through a market-based division of labor, Mises argued, are not limited to a country's borders. The gains from trade through specialization extend to all corners of the globe. Hence, the classical-liberal ideal is inherently *cosmopolitan*. Aggressive nationalism, in Mises's view, not only threatens to bring death and destruction through war and conquest, but it also denies all men the opportunity to benefit from productive intercourse by imposing trade barriers and various other restrictions on the free movement of goods, capital, and people from one country to another. Prosperity and progress are artificially constrained within national boundaries. This perversely can create the conditions for war and conquest as some nations conclude that the only way to obtain the goods and resources available in another country is through invasion and violence. Eliminate all trade barriers and restrictions on the free movement of goods, capital, and men, and limit governments to the securing of each individual's life, liberty, and property, and most of the motives and tensions that can lead to war will have been removed.

Eliminate all restrictions on the free movement of goods, capital, and men, and most of the tensions that can lead to war will have been removed.

Mises also suggested that many of the bases for civil wars and ethnic violence would be removed if the right of self-determination were recognized in determining the borders between countries. Mises took great care to explain that by "self-determination" he did not mean that all those belonging to a particular racial, ethnic, linguistic, or religious group are to be forced into the same nation-state. He clearly stated that he meant the right of individual self-determination through plebiscite. That is, if the individuals in a town or region or district vote to join another nation, or wish to form their own independent country, they should have the freedom to do so.

There still may be minorities within these towns, regions, or districts, of course, that would have preferred to remain part of the country to which they belonged, or would have preferred to join a different country. But however imperfect self-determination may be, it would at least potentially reduce a good amount of the ethnic, religious, or linguistic tensions. The only lasting solution, Mises said, is the reduction of government involvement to those limited classical-liberal functions, so the state may not be used to impose harm or disadvantage on any individual or group in society for the benefit of others.[14]

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Liberalism and the Social Good

Finally, Mises also discussed the question: for whose benefit does the classical liberal speak in society? Unlike virtually all other political and ideological movements, liberalism is a social philosophy of the common good. Both at the time when Mises wrote many of his works and now, political movements and parties often resort to the rhetoric of the common good and the general welfare, but in fact their goals are to use the power of government to benefit some groups at the expense of others.

Government regulations, redistributive welfare programs, trade restrictions and subsidies, tax policies, and monetary manipulation are employed to grant profit and employment privileges to special-interest groups that desire positions in society they are unable to attain on the open, competitive market. Corruption, hypocrisy, and disrespect for the law, as well as abridgments on the freedom of others, naturally follow.

What liberalism offers as an ideal and as a goal of public policy, Mises declared, is an equality of individual rights for all under the rule of law, with privileges and favors for none. It speaks for and defends the freedom of each individual and therefore is the voice of liberty for all. It wants every person to be free to apply himself in the pursuit of his own goals and purposes, so he and others can benefit from his talents and abilities through peaceful market transactions. Classical liberalism wants elimination of government intervention in human affairs so political power is not abusively applied at the expense of anyone in society.[15]

Mises was not unaware of the power of special-interest-group politics and the difficulty of opposing the concentrated influence of such groups in the halls of political power.[16] But he insisted that the ultimate power in society resides in the power of ideas. It is ideas that move men to action, that make them bare their chests at barricades, or that embolden them to oppose wrong-headed policies and resist even the strongest of vested interests. It is ideas that have achieved all the victories that have been won by freedom over the centuries.

Neither political deception nor ideological compromise can win liberty in the twenty-first century. Only the power of ideas, clearly stated and forthrightly presented, can do so. And that is what stands out in Mises's books and makes them one of the enduring sources of the case for freedom.

When Mises wrote many of his books in the 1920s, 1930s, and 1940s, communism and fascism seemed irresistible forces in the world. Since then, their ideological fire has been extinguished in the reality of what they created and the unwillingness of tens of millions to live under their yoke. Nonetheless, many of their criticisms of the free market continue to serve as the rationales for the intrusions of the interventionist welfare state in every corner of society.[17] And many of the contemporary arguments against "globalization" often resemble the criticisms leveled against free markets and free trade by European nationalists and socialists a hundred years ago.[18]

Mises's arguments for individual freedom and the market economy in the pages of *Socialism*, *Liberalism*, *Critique of Interventionism*, *Omnipotent Government*, *Bureaucracy*, *Planned Chaos*, *Human Action*, and many others continue to ring true and remain relevant to our own times. It is what makes his works as important now as when he wrote them across the decades of the twentieth century.

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1. Ludwig von Mises, *Socialism: An Economic and Sociological Analysis* (Indianapolis: Liberty Classics, 1981 [1922; revised eds., 1932, 1951]), pp. 256–78; and *Human Action: A Treatise on Economics*, 4th rev. ed. (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996 [1966]), pp. 143–76.

2. Mises, *Human Action*, pp. 628–34.

3. Ludwig von Mises, "Economic Calculation in the Socialist Commonwealth" [1920], in F.A. Hayek, *Collectivist Economic Planning: Critical Studies on the Possibilities of Socialism* (London: George Routledge & Sons, 1935), pp. 87–130, reprinted in Israel M. Kirzner, ed., *Classics in Austrian Economics: A Sampling in the History of a Tradition*, vol. 3 (London, William Pickering, 1994), pp. 3–30, and Mises, *Socialism*, pp. 95–194; *Bureaucracy* (New Haven, Conn.: Yale University Press, 1944), pp. 20–56; *Human Action*, pp. 689–715; also Richard M. Ebeling, "Why Socialism Is 'Impossible,'" *The Freeman*, October 2004, pp. 8–12.

4. Mises, *Socialism*, p. 102; *Liberalism: The Classical Tradition* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996 [1927]), p. 74; *Omnipotent Government: The Rise of the Total State and Total War* (New Haven, Conn.: Yale University Press, 1944), p. 55; *Bureaucracy*, pp. 58–59; *Planned Chaos* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1947), p. 84; *Human Action*, pp. 258–59, 702–703.

5. Ludwig von Mises, "On the Development of the Subjective Theory of Value" [1931] *Epistemological Problems of Economics* (New York: New York University Press, 1981 [1933]), p. 157.

6. Mises, *Critique of Interventionism* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996 [1929]), pp. 1–31,

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97–106; *Interventionism: An Economic Analysis* (Irvington-on-Hudson, N.Y.: Foundation for Economic Education, 1996 [1941]); *Human Action*, pp. 716–79; *Planning for Freedom* (South Holland, Ill: Libertarian Press, 4th ed., 1980 [1952]), pp. 1–49.

7. Ludwig von Mises, *The Theory of Money and Credit* (Indianapolis: Liberty Classics, 1981 [1912; rev. eds., 1934, 1953]); "Monetary Stabilization and Cyclical Policy" [1928] reprinted in Kirzner, ed., *Classics in Austrian Economics*, vol. 3, pp. 33–111; *Human Action*, pp. 398–478, 538–86, 780–803.

8. For Mises's analysis of the causes and cures for the Great Depression, see Ludwig von Mises, "The Causes of the Economic Crisis" [1931] in Greaves, ed., *Ludwig von Mises, On the Manipulation of Money and Credit*, pp. 173–203; and on Keynesian Economics, see Mises, "Stones into Bread, The Keynesian Miracle" [1948] and "Lord Keynes and Say's Law" [1950], in *Planning for Freedom*, pp. 50–71; for a detailed comparison of the Austrian and Keynesian analyses of the Great Depression, see Richard M. Ebeling, "The Austrian Economists and the Keynesian Revolution: The Great Depression and the Economics of the Short-Run" in Richard M. Ebeling, ed., *Human Action: A 50-Year Tribute* (Hillsdale, Mich.: Hillsdale College Press, 2000), pp. 15–110.

9. See Ebeling, *Austrian Economics and the Political Economy of Freedom* (Northampton, Mass.: Edward Elgar, 2003), chapter 5, "Ludwig von Mises and the Gold Standard," pp. 136–58.

10. *Socialism*, pp. 58–73; *Liberalism*, pp. 18–42; *Human Action*, pp. 150–53, 264–89.

11. Mises, *Liberalism*, p. 55.

12. Mises, *Human Action*, pp. 664–88; *Theory and History*, pp. 44–61; and, Henry Hazlitt, *The Foundations of Morality* (Irvington-on-Hudson, N.Y., Foundation for Economic Education, 1998 [1964]), pp. 55–61. See also Leland B. Yeager, *Ethics as Social Science: The Moral Philosophy of Social Cooperation* (Northampton, Mass.: Edward Elgar, 2001), pp. 81–97.

13. Mises, *Human Action*, pp. 664–88.

14. Mises, *Nation, State, and Economy: Contributions to the Politics and History of Our Time* (New York: New York University Press, 1983 [1919]), pp. 31–56; *Liberalism*, pp. 105–21; *Omnipotent Government*, pp. 79–93.

15. Mises, *Liberalism*, pp. 155–87.

16. See, for example, his essay, "The Clash of Group Interests" [1945] reprinted in Ebeling, ed., *Money, Method and the Market Process: Essays by Ludwig von Mises* (Norwell, Mass.: Kluwer Academic Press, 1990), pp. 202–14.

17. Richard M. Ebeling, "Is the 'Specter of Communism' Still Haunting the World?" *Notes from FEE*, March 2006.

18. See Jerry Z. Muller, *The Mind and the Market: Capitalism in Modern European Thought* (New York: Alfred A. Knopf, 2002), and Ian Buruma and Avishai Margalit, *Occidentalism: The West in the Eyes of Its Enemies* (New York: Penguin Press, 2004).

The essential teaching of liberalism is that social cooperation and the division of labor can be achieved only in a system of private ownership of the means of production, i.e., within a market economy. All the other principles of liberalism—democracy, personal freedom of the individual, freedom of speech and of the press, religious tolerance, peace among nations—are consequences of this basic postulate. They can be realized only within a society based on private property.

—Ludwig von Mises

Omnipotent Government (1944)

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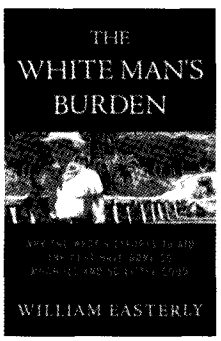
Book Reviews

The White Man's Burden: Why the West's Efforts to Aid the Rest Have Done So Much Ill and So Little Good

by William Easterly
Penguin Press • 2006 • 436 pages • $27.95

Reviewed by Richard M. Ebeling



In his inaugural address in January 1949, President Harry S. Truman made the case for foreign aid to underdeveloped countries. This became known as the "Point Four" program. He argued that those nations could not escape poverty and the threat of communism unless the West and, particularly, the United States undertook an expensive program of financial assistance for capital investment to governments in Latin America, Asia, and Africa.

In 1950 FEE published a monograph by free-market journalist Henry Hazlitt titled *Illusions of Point Four.* He argued, "We are much more likely to strengthen the fabric of world peace by letting private capital go to those regions that have built up the confidence of foreign investors by respecting their contracts, by respecting the legal rights of persons and private property, by creating an atmosphere of internal peace and order, and by refraining from socialization, nationalization, militarization, and all the other totalitarian symptoms that go with external aggressiveness."

To make it attractive for private-sector foreign investment, Hazlitt stated, "The real reforms must come from within each country. . . . Each would-be borrowing country must make itself credit-worthy. It must inspire or regain the confidence of the private foreign investor. It can do this only by adopting or restoring a truly liberal economic policy" of free markets, rule of law, free trade, and limited government.

For more than half a century, the U.S. and European governments, and the international organizations they dominate, including the IMF and the World Bank, have chosen the path of international redistribution of wealth through politically funded foreign aid. The result has been one disaster after another.

A few voices were raised in defense of market solutions to global poverty, especially that of the late Peter Bauer. But the general presumption over more than five decades has been that only governments can guide humanity to prosperity. One recent and insightful voice on the negative effects of government-to-government aid has been William Easterly, a former economist with the World Bank. Easterly's new book, *The White Man's Burden*, dissects the harm that has been done by these government programs.

He begins by suggesting that the world may be divided into two types of mentalities: Planners and Searchers. Planners always assume they know the solution to other people's problems and can design grand plans to remake society and its institutions. Searchers are the rest of us, who try to find ways in our individual corners of society to improve our circumstances through exchange and association through the division of labor.

Easterly argues that policymakers, too, can be Searchers, but only if they start from the premise that no one has the knowledge and ability to micromanage society. Instead, they look for ways to improve the institutions through which individuals will be better able to solve the local problems the Planner can never fully understand.

Easterly points out that Planners live in a linguistic fantasyland, deluding themselves and others about what they do and with whom they interact in less-developed countries. In a version of George Orwell's "Newspeak," Planners refer to war as "conflict-related reallocation of resources." Working with mass-murdering dictators becomes "difficult partnerships." A country where the tyrant loots the wealth of the society is called "governance issues." When local politicians and bureaucrats try to steal the targeted foreign aid, this becomes "differences in priorities and approaches."

Chapter after chapter details examples of foreign aid that went into political pockets, was "reallocated" to serve the ends of those in power, was wasted on high-profile investment projects that served no rational economic purpose, undermined the ability of the citizens of

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these countries to improve themselves, or actually brought about a regression in the economic condition of the population.

Easterly also hammers home the key point that the incentives of the foreign-aid providers usually have little or no relation to the needs of the people in whose name they squander tens of billions of dollars. To maintain their jobs, budgets, and comfortable lifestyle as global paternalists, they must impress the politicians and voters in their home countries who provide the largess on which they live. Their first priority is generating big goals, extravagant international conferences, major global "reports," impressive statistics, and assurances that prosperity would be just around the corner for these parts of the world—if only more money were allocated to their tender care.

Peacekeeping efforts by the UN and NATO, and the attempts to introduce democracy by selecting or propping up existing political leaders, have had few successes, Easterly argues. Social, political, and economic change, if it is to be permanent and stable, must come from within these countries; it cannot be imposed by an outside power, no matter how well-intentioned that power may view itself to be. The "white man's burden" of nineteenth- and early-twentieth-century colonialism left few success stories when the colonial power's flag was lowered.

If this second version of the white man's burden in the form of Western foreign aid also has been a failure, then what can help end the poverty and misery in these unfortunate countries? Easterly gives many examples of local and private avenues to investment, industry, and commerce that slowly but surely have been bringing about improved standards of living in Asia, Africa, and Latin America.

These efforts have worked most effectively when aid and investment have focused on the circumstances and abilities of the people themselves, and not on the grand visions of the Planners. The heart of the matter, as Easterly emphasizes over and over again, is the fostering of homegrown market economies that reflect the culture and history of the local population. It must be realized, as well, that societal change does not happen overnight; nor will it be a simple carbon copy of the institutions we take for granted in the West.

Finally, it should be pointed out that Easterly is not a consistent advocate of free-market solutions to development problems. While he believes that the private sector is the core of change and improvement, he thinks that it might be possible to devise some foreign-aid programs complementary to its efforts.

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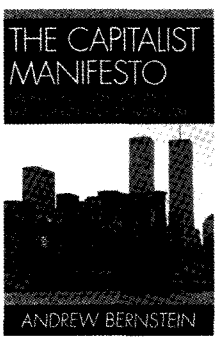
The Capitalist Manifesto

by Andrew Bernstein

University Press of America • 2005 • 394 pages

$37.00 paperback

Reviewed by Gary M. Galles



Andrew Bernstein's *The Capitalist Manifesto* claims to set forth the historic, economic, and philosophical case for laissez faire. It succeeds on the first two counts, but falters on the third.

The book begins by contrasting capitalism, based on "the fundamental moral principle . . . that individuals have inalienable rights and that governments exist solely to protect those rights," with statism, "the subordination of the individual to the state."

Bernstein, who teaches philosophy at Pace University, then debunks the false, but long-held claims that capitalism harmed workers, and does so in a manner that should be convincing to all but those determined not to believe. He shows how after centuries of economic stagnation, capitalism and the Industrial Revolution wrought an unprecedented and undreamed-of rise in living standards. History also demonstrates that freer countries prosper relative to less-free neighbors (for example, North versus South Korea) and that growth within a country increases with the extent of freedom (for example, the United States and Sweden).

The Capitalist Manifesto refutes other false accusations against capitalism. It shows that harmful monopolies result from government interference with the free market. The book connects excess unemployment to coercive government labor-market restrictions. Inflation and

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depression are similarly tied to government actions. While not breaking new ground, it provides a valuable account of how alleged "evils of capitalism" actually originate from its absence.

Bernstein also presents as heroic those individuals who created and developed the ideas that dramatically improved people's lives. This "hero worship" is interesting but is not essential to the core argument that only capitalism, by not hamstringing entrepreneurs with restrictions, allows such mutual flourishing.

Unfortunately, when it comes to the basis for Bernstein's minimal-state conclusions (conclusions I share), the book founders. He presents Ayn Rand's Objectivist philosophy as *the* dramatic breakthrough allowing people to finally see that laissez-faire capitalism is the only moral economic system. Despite recognizing Rand's importance as a leading twentieth-century advocate of liberty, especially able at highlighting statist assumptions behind policies, I found it unconvincing.

The claims made for Rand's "breakthrough" overreach. For instance, the American Revolution is attributed to implicit understanding of her egoism-based philosophy. But that belief in self-ownership and the principles of liberty was religiously based, which contrasts sharply with Rand's hostility to religion as substituting emotionalism for rational thought. Further, since self-ownership and liberty were similarly understood two centuries ago (for example, Samuel Adams's assertion that "Men's rights are evident branches of, rather than deductions from, the duty of self-preservation"), it seems that Rand primarily made the same claims, just leaving out religion.

The logic presented is sometimes short of rigorous. Sweeping language is often used to generate similarly sweeping conclusions, when more measured language would be appropriate. Broader conclusions are drawn than are justified deductively, such as that since we need to use our minds to advance our lives, *no* restrictions on their use can be justified, or considering it proven that since freer countries have prospered more than less-free counterparts, laissez-faire government would necessarily yield still better results (likely, but not proven).

Perhaps the book's greatest problem is its assertion that Rand's egoism is the only moral basis on which capitalism can be defended. That is incorrect. Capitalism is clearly defensible on Christian principles, and most historical defenses of liberty employed Christian, not egoistic, rationales. The book's assertion implies that a Christian could not accept capitalism without rejecting Christianity, which will undermine far more believers in liberty than it will win. I think that asserting self-ownership, "Thou shalt not murder (kill)" and "Thou shalt not steal," are sufficient to justify capitalism, without the unclear distinctions and attacks on those who don't agree.

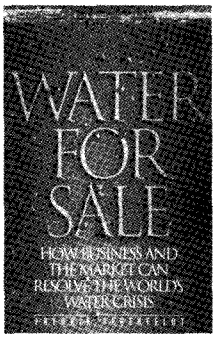
Despite an unconvincing assertion of Ayn Rand's philosophy as the sole moral basis for capitalism and some presentation problems (including repetitious and irritating uses of unattributed quotations), *The Capitalist Manifesto* is a useful presentation of the economic and historical case for capitalism. But I fear the harsh tone of the philosophical discussion, reflecting the similar tone often used by Rand, risks keeping away many who would benefit from the book.

Gary Galles (Gary.Galles@Pepperdine.edu) is a professor of economics at Pepperdine University.

Water for Sale: How Business and the Market Can Resolve the World's Water Crisis

by Fredrik Segerfeldt
Cato Institute • 2005 • 118 pages • $12.95 paperback

Reviewed by George C. Leef



Ask someone to name the essentials for life and almost certainly the first two words he'll say will be food and water. All but the most strident leftist accepts that food is best produced and distributed through the free market, but many people insist that government must step in to ensure everyone enough clean water, either "free" or at "reasonable" prices. The idea of leaving water to the market evidently frightens many into advocating water socialism.

Socialism, as Ludwig von Mises so cogently demonstrated, *necessarily* makes people worse off by leading to inefficiency and the retarding of progress. The conse-

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quences are most dire for people living at the margin of existence, and especially so when the commodity in question is one as crucial as water. In *Water for Sale* Fredrik Segerfeldt argues that poor people around the globe are suffering because of government water monopolies and that they would be far better off with provision by the free market. Segerfeldt, a senior adviser to the Confederation of Swedish Enterprise (the book was originally published in Swedish by the think tank Timbro), points out that more than a billion people do not have what Americans take for granted—abundant supplies of clean water. Approximately 12 million deaths per year can be attributed to the lack of clean water. One would think that a problem of that magnitude would cause "social activists" around the world to battle for the replacement of ineffective government water systems with market alternatives.

But that's not the case at all. Segerfeldt documents the vociferous opposition that proposals for abandoning socialism for private enterprise in water provoke. He writes, "Opponents of privatization look askance at the possibility of making money from people's need for water and fear that the poor will have this fundamental necessity taken away from them if they cannot pay for it. Water, they argue, is a human right that the public sector is duty-bound to provide."

That opposition is strong even though there have been many success stories with water privatization. For example, Segerfeldt notes that in Manila private enterprise had a tremendous positive effect when businessmen were allowed to establish a water company. People who had been getting water for only a few hours a day at high prices from the government system report that they now have access to water around the clock, and at lower prices. How much lower? Where a cubic meter of water used to cost 100 pesos, it is now only 15 pesos—a huge saving for a poor family.

Who are these vociferous opponents? Predictably, public-sector workers who enjoy their monopoly use all their political clout to oppose any move toward a free market in water. They find allies in various nongovernment organizations that reflexively oppose any measure with a hint of capitalism, and in the media, which usually give abundant coverage to the political/ideological foes of the free market. Segerfeldt writes with passion that "it would be not just a pity, but quite outrageous if millions of people were to starve, fall ill, and die through water shortages brought about by the strident propaganda of vested interests and powerful ideological movements with different ends in view."

Showing the typical leftist preference for shared misery rather than capitalist abundance, opponents of water privatization often contend that since there isn't enough water to go around, our emphasis should be on reducing water usage instead of increasing its supply. Segerfeldt crushes that idea in his chapter "A Shortage of Good Policies, Not of Water."

In the course of the book the author indicts the governments of poor countries where water supply is so deficient. The priorities of the rulers and their supporters are such that clean water for ordinary people is of little importance. It's an old, sad story that needs to be told again and again: Those who run governments should be counted on to do what is in *their* interest, not what is in the interest of the mass of the population.

Water for Sale is chock full of evidence of the success of free-market water projects and the failures of water socialism. The book is remarkably effective in demonstrating that supposedly cold-hearted capitalism does wonders for poor people when it's allowed to function, and also that the supposedly compassionate advocates of statism are committed to policies that help keep the poor mired in poverty and misery.

So let's hoist a glass of water—or any other beverage you choose—to Fredrik Segerfeldt for this enlightening book.

George Leef (georgeleef@aol.com) is the book review editor of The Freeman.

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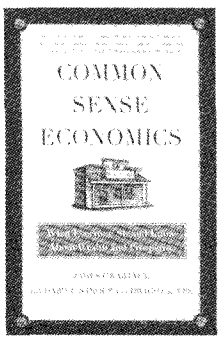
Common Sense Economics: What Everyone Should Know About Wealth and Prosperity

by James Gwartney, Richard L. Stroup, and Dwight R. Lee
St. Martin's Press • 2005 • 194 pages • $18.95

Reviewed by Tom Lehman



It is often said that common sense is not all that common. Another adage heard by economists is that economics is the "painstaking elaboration of the obvious." Such clichés were happily ignored by the authors of *Common Sense Economics.* They give the reader dose after dose of common-sense economic analysis while taking the pain out of understanding not-always-so-obvious insights into how markets work. Gwartney, Stroup, and Lee have taken seriously the call for economic literacy, with the intent of making economics intelligible for the wider audience. If you are a student, a business professional, or just curious about the world and want to understand economics, this book is for you. If you are an instructor of economics, the book makes an excellent supplement to traditional principles texts.

The main theme throughout the book will be familiar to readers of *The Freeman*: economic performance depends critically on getting the incentives right, and private property, free enterprise, and minimal government intervention are the most effective means of harnessing incentives for the betterment of all. The authors know their economics and are gifted apologists for the "invisible hand." They carefully lead the reader down a narrow path, avoiding both technical economic research and the half-truths of contemporary economic populism, all in a reader-friendly prose devoid of graphs and equations. As the authors themselves say in the preface, readers armed with the simple yet powerful tools of economic logic "will be better able to differentiate between sound arguments and economic nonsense."

The book is tightly organized into four chapters. The authors preface each with a condensed list of the topics to be discussed. For example, chapter one, "Ten Key Elements of Economics," begins with a list of standard economic principles including: incentives matter, no free lunches, and people earn income by helping others. Likewise, chapter three, "Economic Progress and the Role of Government," begins with a similar list, including: government is not a corrective device, the costs of government are not only taxes, and central planning replaces markets with politics. These brief lists at the outset of each chapter significantly enhance the readability of the book. They will be especially helpful as a reference to students reviewing the book in preparation for their first economics exam.

Perhaps the book's most impressive feature is its breadth (despite its conciseness) without distracting economic terminology. From Adam Smith to John Maynard Keynes to F. A. Hayek, Milton Friedman, and James Buchanan, the key ideas of the major contributors in economics are made accessible to the lay person, always with the intention of helping the reader appreciate the forces of the free-market process. For example, in the first chapter, the authors link the importance of pricing signals to the efficient employment of scarce resources by exposing readers to Adam Smith's "invisible hand": prices encourage individuals to employ scarce resources in a way that improves the well-being of society, even though they intended only to further their own interests. The authors then dovetail this concept into a discussion of Hayek's "knowledge problem" by explaining how prices guide millions of people to cooperate anonymously with one another in the carrying out of their individual plans. In about three paragraphs the authors distill the salient points of Hayek's 1945 scholarly article "The Use of Knowledge in Society."

One thing that concerns me is the difference between accessibility and "dumbing down" in the worthy effort to promote economic literacy. The authors do a wonderful job of speaking "jargon-free" economics, placing conventional economic terms in a simple glossary at the end of the book. However, as an economics educator, I find at least some of that jargon useful in conveying a deeper understanding of certain topics ("elasticity" for example). Even the term "opportunity cost" is relegated only to the glossary. One wonders if the message the authors gracefully communicate might not possess greater staying power if a few more of those terms had been introduced.

The authors are clearly passionate about reaching a

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wider audience and improving economic literacy. They comprehend, as any dedicated economist does, that only when voter-consumers understand economics will they be inoculated against the bad ideas and half-truths that frequently lend support to wealth-destroying government policies. As the authors proclaim, a "nation of economic illiterates is unlikely to remain prosperous for very long." Nor, one might add, is it likely to remain free. In this book, Gwartney, Stroup, and Lee have perhaps done for current and future generations what Henry Hazlitt's classic, *Economics in One Lesson*, did for past: illustrate the compelling logic of economics in an accessible format that is enjoyable and intellectually enriching, while also respecting the reader's time constraints.

Tom Lehman (Tom.Lehman@indwes.edu) is an associate professor of economics at Indiana Wesleyan University.

Coming in the July-August *Freeman*

Democracy versus Liberty
by James Bovard

The Anatomy of Economic Advice
by Israel M. Kirzner

Wartime Executive Power:
Are Warrantless Wiretaps Legal?
by Robert A. Levy

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The End Run to Freedom

BY RUSSELL ROBERTS

What does the future hold for economic life in the United States? Will we move toward greater freedom or less? What role will ideas and rhetoric play, if any, in making sure that the direction is one that lovers of freedom prefer?

One way of looking at American economic policy in the twentieth century is that Keynes held sway over economic policy for the first 50 years. In the second half of the twentieth century, Milton Friedman and F. A. Hayek held the upper hand. In the first half of the twentieth century the dominant president was FDR, who centralized economic power. In the second half of the twentieth century the most important president from the perspective of economic policy was Ronald Reagan, whose advocacy of smaller government and antipathy to the Soviet Union spread the use of market forces in the United States and beyond, to Eastern Europe and Latin America. One could argue that the increased market orientation of the Chinese economy is part of this trend. In this story of the twentieth century and the future, the glass is half full.

But perhaps the glass is half empty. Government spending continues to grow. The limited government that Reagan espoused was more rhetoric than reality—the era of big government is clearly not over. In fact, government continues to grow and at an increasing rate of late. Even the rhetoric has faded now; few politicians seriously advocate real economic freedom. Even George Bush's plan for "privatizing" Social Security required forced saving administered by the government.

So what's a classical liberal to think? Is there any reason for optimism? My colleague and blogger extraordinaire Tyler Cowen thinks not, at least in the short run:

> My prediction is that, in general, welfare states will increase in size in most places around the world. We can expect most areas of the world to become wealthier because of globalization as well as other reasons. And if you look at countries that are wealthy, they tend to have very generous welfare states. Also, I believe that the human desire for security is extremely strong, even when it is not efficient or rational. So as long as we experience economic growth, I think we can expect welfare states to grow. ("Interview, Tyler Cowen," *Region Focus*, Winter 2006)

Tyler seems right. All evidence points to an increasingly centralized world, a world where taxes are higher, where welfare states are bigger, where individual liberty, at least economic liberty, is smaller. And the fundamental reason is that as we get wealthier, we buy more of the things we like. One thing we like is security. When you're poor, a risk-free or less risky world is a luxury. When you get richer, you take more care and caution because you can afford to.

This effect of higher incomes on behavior is one reason, I suspect, that parenting today isn't what it used to be. We make our children wear bike helmets; we program them so that they don't roam freely in the neighborhood; and we discourage risky activity in a way previous generations never did.

That desire for security and less risk funds the welfare state in America. That desire for security and less risk creates a seemingly never-ending demand for protectionism. That desire for security and less risk creates the nanny state—the regulatory environment that makes seat belts, tobacco, cocaine, and prescription drugs the government's business when it should be mine and mine alone.

If Tyler is right, as other nations get wealthier, they will become more like the United States in how they treat risk. The increased wealth will create a demand for regulation just as it has in the United States. And future

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growth in the United States will create even more paternalistic regulations here.

Could be. I might even wager that Tyler's right. But I hope he's wrong. And I can imagine at least one route to economic freedom, despite all the trends running in the other direction.

As we get wealthier, we do want more safety and security. That trend isn't going to change. But why do that safety and security have to come from the government? Why can't we get our safety and security from private, voluntary sources? The obvious answer is that that trend is also running in the wrong direction—we turn increasingly to the government for achieving the goals of security. We're further from abolishing the FDA than ever before. We're banning smoking in private restaurants in some cities and more are on the way.

But on the positive side, we're closer to abolishing Social Security than ever before. Not very close, admittedly, but closer. True, President Bush's privatization wasn't real privatization, but it was closer to real privatization than expanding the government's role in Social Security.

As we get richer, two things affect the Social Security debate, both trending toward freedom. First, money coming from private assets will increasingly dwarf those government Social Security checks. And that's even before the system has to cope with the baby boomers, putting downward pressure on benefits. When people talk about the "riskiness" of private Social Security, they conveniently ignore the fact that half the American people own stocks and they like it. An increasing proportion of the American people already controls their retirement money through their own decisions.

The proponents of government-provided retirement always raise the specter of people starving in the street by their myopic failure to save for retirement or simply from bad decisions. But why can't private, voluntary charity take care of those who struggle? The skeptic responds that there's a free-rider problem—people simply will let others take care of the unfortunate. Too many people will step aside to let others take up the burden, and as a result, there won't be enough money to help the poor. We need government, they argue, to tax everybody to provide for the poor elderly who won't have the foresight or the good fortune to be self-sufficient.

Overcoming the Free-Rider Problem

But as America becomes wealthier it will be easier to overcome the free-rider problem to bring the poor out of destitution. That increases people's willingness to try a private solution for taking care of the elderly.

There's a fly in this ointment of freedom. As we get wealthier we'll also have higher standards for what it means to take care of elderly people who are poor. That will push some Americans to keep favoring coercive government solutions. But if enough wealthy Americans fund those private alternatives to government, maybe we can show people that private solutions can actually work.

Call it an end run to freedom. We're already seeing this strategy with educational reform. Instead of waiting for enough Americans to tire of the failure of the public school system and pressure politicians to support vouchers, people have turned down the "free" public schools and home-schooled their kids or sent them to private schools.

And some people have funded scholarships for poor kids to go to private schools. Yes, there's a free-rider problem. But enough people give anyway to make privately funded scholarships a real way to show people that vouchers work, or even better, that we don't need government schools.

As we get wealthier, these private end runs around the heavy hand of government are easier to fund. If we keep fighting the good intellectual fight and making the moral and analytical case for freedom, the end runs can help us market the virtues of freedom to the skeptics. We'll never reduce the demand for security and safety. But maybe, just maybe, we can establish the superiority of private, voluntary solutions to government solutions.

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A FEE Classic Since 1950!

THE LAW

BY FREDERIC BASTIAT

New Introduction by
RICHARD EBELING

Foreword by
WALTER E. WILLIAMS

Afterword by
SHELDON RICHMAN

Published in the last year of his brief, embattled life, *THE LAW* is Bastiat's most famous work—and justly so. A masterpiece of style, brevity, and common sense, *THE LAW* concisely presents the classic moral case for liberty and limited government. With persuasive power and enduring impact, it ranks with the great essays of John Stuart Mill and Thomas Paine. For more than a century, *THE LAW* has been changing the thinking of thousands about the relationship of man and state. Here again is Frederic Bastiat's ringing challenge to the dominant political forces of his day. And our own.

FREDERIC BASTIAT (1801-1850) was a French economist, statesman, and writer. His uncompromising defenses of free trade, the market economy, and individual liberty pitted him against politicians both right and left. His writings include *Economic Sophisms*, which championed free trade; *Economic Harmonies*, a treatise on economic principles, plus a host of essays, including "The State" and "What Is Seen and What Is Not Seen." To this day, his witty aphorisms and incisive arguments are quoted by public figures, speakers, and writers everywhere.

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There is nothing wrong with money that freedom will not cure. This is another way of saying that the Good Society which many reformers have sought by way of monetary reform cannot be achieved that way; if it is ever to be achieved, it will be done by freedom. So, then, the fight for sound money, to have meaning, must be related to the broader fight for freedom. It is only one of the several battles that must be fought.

— Frank Chodorov (1887–1966)

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